

UNITED PARCEL SERVICE INC  
Form 10-K  
February 21, 2019

UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549

Form 10-K  
FOR ANNUAL AND TRANSITION REPORTS  
PURSUANT TO SECTIONS 13 OR 15(d) OF THE  
SECURITIES EXCHANGE ACT OF 1934

(Mark One)

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended December 31, 2018

or

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from \_\_\_\_\_ to \_\_\_\_\_  
Commission file number 001-15451

United Parcel Service, Inc.  
Delaware 58-2480149  
(State or Other Jurisdiction of (I.R.S. Employer  
Incorporation or Organization) Identification No.)  
55 Glenlake Parkway, N.E. Atlanta, Georgia 30328  
(Address of Principal Executive Offices) (Zip Code)  
(404) 828-6000  
(Registrant's telephone number, including area code)

Securities registered pursuant to Section 12(b) of the Act:

Title of Each Class	Name of Each Exchange on Which Registered
Class B common stock, par value \$.01 per share	New York Stock Exchange
Floating-Rate Senior Notes due 2020	New York Stock Exchange
1.625% Senior Notes due 2025	New York Stock Exchange
1% Senior Notes due 2028	New York Stock Exchange
0.375% Senior Notes due 2023	New York Stock Exchange
1.500% Senior Notes due 2032	New York Stock Exchange

Securities registered pursuant to Section 12(g) of the Act:

Class A common stock, par value \$.01 per share  
(Title of Class)

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes  No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Exchange Act. Yes  No

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes  No

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit such files). Yes  No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company or an emerging growth company. See definition of "accelerated filer", "large accelerated filer", "smaller reporting company" and "emerging growth company" in Rule 12b-2 of the Exchange Act. Check one:

Large accelerated	Accelerated	Non-accelerated	Smaller reporting	Emerging growth
filer <input checked="" type="checkbox"/>	filer <input type="checkbox"/>	filer <input type="checkbox"/>	company <input type="checkbox"/>	company <input type="checkbox"/>

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes  No

The aggregate market value of the class B common stock held by non-affiliates of the registrant was \$73,643,493,685 as of June 30, 2018. The registrant's class A common stock is not listed on a national securities exchange or traded in an organized over-the-counter market, but each share of the registrant's class A common stock is convertible into one share of the registrant's class B common stock.

As of February 6, 2019, there were 164,239,863 outstanding shares of class A common stock and 695,989,113 outstanding shares of class B common stock.

**DOCUMENTS INCORPORATED BY REFERENCE**

Portions of the registrant's definitive proxy statement for its annual meeting of shareowners scheduled for May 9, 2019 are incorporated by reference into Part III of this report.

UNITED PARCEL SERVICE, INC.  
ANNUAL REPORT ON FORM 10-K  
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## PART I

### Cautionary Statement About Forward-Looking Statements

This report, our Annual Report to Shareowners and our other filings with the Securities and Exchange Commission (“SEC”) contain certain “forward-looking statements” within the meaning of the Private Securities Litigation Reform Act of 1995. Statements in the future tense, and all statements accompanied by terms such as “believe,” “project,” “expect,” “estimate,” “assume,” “intend,” “anticipate,” “target,” “plan” and variations thereof and similar terms, are intended to be forward-looking statements. Forward-looking statements are made subject to the safe harbor protections of the federal securities laws pursuant to Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934.

From time to time, we also include written or oral forward-looking statements in other publicly disclosed materials. Such statements relate to our intent, belief and current expectations about our strategic direction prospects and future results, and give our current expectations or forecasts of future events; they do not relate strictly to historical or current facts. Management believes that these forward-looking statements are reasonable as and when made. However, caution should be taken not to place undue reliance on any such forward-looking statements because such statements speak only as of the date when made.

Forward-looking statements are subject to certain risks and uncertainties that could cause actual results to differ materially from our historical experience and our present expectations or anticipated results. These risks and uncertainties are described in Part I, “Item 1A. Risk Factors” and may also be described from time to time in our future reports filed with the SEC. You should consider the limitations on, and risks associated with, forward-looking statements and not unduly rely on the accuracy of predictions contained in such forward-looking statements. We do not undertake any obligation to update forward-looking statements to reflect events, circumstances, changes in expectations or the occurrence of unanticipated events after the date of those statements.

### Item 1. Business

#### Overview

United Parcel Service, Inc. (“UPS”) was founded in 1907 as a private messenger and delivery service in Seattle, Washington. Today, we are the world’s largest package delivery company, a leader in the U.S. less-than-truckload industry and a premier provider of global supply chain management solutions. We operate one of the largest airlines in the world, as well as the world’s largest fleet of alternative-powered vehicles. We deliver packages each business day for 1.5 million shipping customers to 9.1 million receivers (“consignees”) in over 220 countries and territories. In 2018, we delivered an average of 20.7 million pieces per day, or a total of 5.2 billion packages. Total revenue in 2018 was \$71.861 billion.

We serve the global market for logistics services, which includes transportation, distribution, contract logistics, ground freight, ocean freight, air freight, customs brokerage, insurance and financing. We have three reporting segments: U.S. Domestic Package and International Package, which together we refer to as our global small package operations, and Supply Chain & Freight, all of which are described below.

#### Strategy

Our market strategy is to provide customers with advanced logistics solutions made possible by a broad portfolio of differentiated services and capabilities expertly assembled and integrated into our customers’ businesses. This approach, supported by our efficient and globally balanced multimodal network, enables us to deliver value to our customers and thereby build lasting partnerships with them.

Customers are able to leverage our broad portfolio of logistics capabilities comprised of: our balanced global presence in North America, Europe, Middle East, Africa, Asia Pacific and Latin America; reliability; and industry-leading technologies and solutions expertise for competitive advantage in markets where they choose to compete.

We continue to invest in the expansion of the UPS business to serve our existing and prospective customers with a full range of advanced logistics products, services and capabilities across an ever-increasing geographical and industry footprint. Achieving our objectives has required new methods and innovative approaches to logistics services, including the acquisition and creation of platform-based businesses, specialized healthcare services such as Marken's clinical trial capabilities, a full range of brokerage and transportation insurance services, retail offerings such as UPS My Choice and more.

We have a long history of operating with joint venture and partnership arrangements to provide flexibility as we build scale. We often reevaluate these arrangements to ensure they are optimally designed for our future aspirations. For example, in 2018, we acquired full ownership of our express services unit in India, signaling a new era of opportunity and operational design in a high-growth international market. We closely monitor global trade and economic, geopolitical, regulatory and environmental factors, as well as other areas of risk and change to ensure we quickly adjust to a fast-moving world.

We aim to be a disciplined and focused business that purposefully reinvests capital to achieve both long-term strategic benefits and favorable returns. In September 2018, we communicated our commitment to continuous transformation to modernize our business and operations through state-of-the-art technology. We see transformation as an ongoing commitment to enhance quality and efficiency as we deliver innovative capabilities and services. Our strategic investments are primarily focused in areas we believe will drive growth and lasting profit potential:

• Services and solutions for small and medium-sized businesses.

• International growth markets.

• Global Business to Consumer (“B2C”) and Business to Business (“B2B”) e-commerce.

• Healthcare and life-sciences logistics.

• Operational advancements and efficiencies through our technology-enabled network.

In 2018, we added nearly 400,000 pieces per hour of automated sort capacity globally, along with numerous new technologies to help control the network and ensure resources are in the right place at the right time.

We have a long history of sound financial management, and our consolidated balance sheet showcases financial strength. Cash generation is a significant strength of UPS, giving us ample capacity to service our obligations and facilitate distributions to shareowners, reinvest in our business and pursue growth opportunities.

## Reporting segments and products & services

### Global Small Package

Our global small package operations provide time-definite delivery services for express letters, documents, small packages and palletized freight via air and ground services. We serve more than 220 countries and territories around the world along with domestic delivery service in more than 50 countries. We handle packages up to 108 inches in length that weigh up to 150 pounds and are up to 165 inches in combined length and girth, as well as palletized shipments weighing more than 150 pounds. All of our package services are supported by numerous shipping, visibility and billing technologies.

We handle all levels of service (air, ground, domestic, international, commercial and residential) through one global integrated pickup and delivery network. We combine all packages within our network, unless dictated by specific service commitments. This enables one UPS driver to pick up customers’ shipments for any of our services at the same scheduled time each day. Compared to companies with single service network designs, our integrated network uniquely provides operational and capital efficiencies while being more environmentally friendly.

We offer same-day pickup of air and ground packages upon request. Customers can schedule pickups up to six days a week, based on their specific needs. Additionally, our wholly-owned and partnered global network offers roughly 150,000 entry points where customers can tender a package to us at a location or time convenient to them. This combined network includes UPS drivers who can accept packages provided to them, UPS drop boxes, UPS Access Point locations, The UPS Store locations, authorized shipping outlets and commercial counters, alliance locations and customer centers attached to UPS facilities. Some of these locations offer a full array of services, including pickup, delivery and packing options, while others are drop-off locations only.

The continued growth of online and mobile shopping has increased our customers' needs for efficient and reliable returns, resulting in our development of a robust selection of returns services that are available in more than 145 countries. The portfolio provides a range of cost-effective label options and a vast network of consumer drop points, as well as a selection of returns technologies that promote efficiency and a friction-free consumer experience. These options vary based on customer need and country and include solutions such as UPS Returns, as well as more-specialized services such as UPS Returns Exchange. Our technologies promote systems integration, client ease of use and visibility of inbound merchandise, which help reduce costs and improve efficiency of our merchants' reverse logistics processes. UPS Returns Manager is an excellent example of this value.

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We operate one of the largest airlines in the world, with global operations centered at our Worldport hub in Louisville, Kentucky. Worldport sort capacity has expanded over the years due to volume growth and centralization efforts. Our European air hub is located in Cologne, Germany, and we maintain Asia Pacific air hubs in Shanghai, China; Shenzhen, China and Hong Kong. Our regional air hub in Canada is located in Hamilton, Ontario and our regional air hub for Latin America and the Caribbean is in Miami, Florida.

Our U.S. regional air hubs in Dallas, Texas; Ontario, California; Philadelphia, Pennsylvania and Rockford, Illinois support Worldport. This network design creates cost-effective package processing in our most technology-enabled facilities, which allows us to use fewer, larger and more fuel-efficient aircraft. Our U.S. ground fleet serves all business and residential zip codes in the contiguous U.S.

#### U.S. Domestic Package Reporting Segment

We are a leader in time-definite, money-back guaranteed, small package delivery services in the United States. We offer a full spectrum of U.S. domestic guaranteed ground and air package transportation services.

Customers can select from same day, next day, two day and three day delivery alternatives. UPS's Air portfolio offers options enabling customers to specify a time-of-day guarantee for their delivery (e.g., by 8:00 A.M., 10:30 A.M., noon, end of day, etc.).

Customers can also leverage our extensive ground network to ship using our day-definite guaranteed ground service that serves every U.S. business and residential address. We deliver more ground packages in the U.S. than any other carrier, with average daily package volume of 14.5 million, most within one to three business days.

We also offer UPS SurePost, an economy residential ground service for customers with non-urgent, lightweight residential shipments. UPS SurePost is a contractual residential ground service that combines the consistency and reliability of the UPS Ground network with final delivery often provided by the U.S. Postal Service. We utilize our operational technology to identify multiple package delivery opportunities and redirect UPS SurePost packages for final delivery, improving time in transit, customer service and operational efficiency.

We continue to invest in our smart global logistics network. Within our facilities, we are expanding automated capacity, driving greater efficiencies and providing additional network flexibilities. We also continue to invest in our air network capacity through aircraft acquisitions. In 2018, we expanded Saturday operations and opened 22 new facilities, including regional facilities in the Atlanta, Indianapolis, Phoenix, Salt Lake City and Dallas areas.

#### International Package Reporting Segment

Our International Package reporting segment includes small package operations in Europe, Asia Pacific, Canada and Latin America and the Indian sub-continent, Middle East and Africa ("ISMEA"). We offer a wide selection of guaranteed day- and time-definite international shipping services. We offer more guaranteed time-definite express options (Express Plus, Express and Express Saver) than any other carrier.

In 2018, we continued expansion of our Express time-definite portfolios:

We expanded UPS WorldWide Express to 14 new countries around the globe.

UPS Express now reaches 137 countries with guaranteed mid-day delivery and 57 countries with guaranteed morning delivery with Express Plus.

Express Saver reaches 220 countries and territories with guaranteed end-of-day delivery.

We grew our Worldwide Express Freight Midday footprint by five times in 12 European countries by expanding this service to 39,000 new postal codes.

Worldwide Express Freight is available from 71 origin countries to 67 destination countries.

For international package shipments that do not require Express services, UPS Worldwide Expedited offers a reliable, deferred, guaranteed day-definite service option. The service is available from more than 80 origin countries to more than 220 countries and territories.

For cross-border ground package delivery, we offer UPS Standard delivery services within Europe, between the U.S. and Canada and between the U.S. and Mexico.

Europe, our largest region outside of the U.S., accounts for approximately half of international revenue and is one of the primary drivers of our growth. To accommodate the strong potential for growth in small package exports, we made a series of enhancements to both our ground and air networks that help reduce transit time by one to two days and will result in improved exporting opportunities for customers in Europe.

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We are constantly striving to provide our customers with better service. In 2018, we provided our customers with greater flexibility by offering later pick-up times in nearly 52,000 postal codes across Europe, creating production and fulfillment benefits. We continue to make major European infrastructure investments, including a \$146 million facility in Eindhoven, the Netherlands, the opening of a \$150 million hub in London and the construction of a \$100 million hub in Paris. These investments are part of ongoing efforts allowing customers using UPS Standard to reach more than 80 percent of Europe's population within two business days. These recent expansions and enhancements are part of our commitment to invest nearly \$2 billion in our European infrastructure.

Asia Pacific remains a strategic market due to growth rates in intra-Asia trade and the expanding Chinese economy. To capitalize on these opportunities, we are bringing faster time-in-transit to customers focused on intra-Asia trade and reducing transit time from Asia to the U.S. and Europe. Through added flight frequencies, we provide our customers the ability to ship next day to more places in the U.S. and Europe - guaranteed - than any other express carrier. We serve more than 40 Asia Pacific countries and territories through more than two dozen alliances with local delivery companies that supplement company-owned operations. Our joint venture with SF Express combines SF's extensive Chinese network with UPS's delivery capabilities in the U.S. and Europe to increase our market presence and help provide Chinese enterprises with greater global access.

In 2018, we extended cut-off times by four hours for export shipment pickups, lengthening production windows. We upsized four daily flights to our Shenzhen Intra-Asia hub and Hong Kong to our new Boeing 747-8s for greater capacity to support customers with import needs through gateways in Shanghai, Shenzhen and Hong Kong. High-growth markets are also a strategic imperative for UPS. A new direct flight from the U.S. to Dubai improves time in transit to key destinations in the ISMEA region for shippers throughout the U.S., Canada and the Americas. Markets like India in the ISMEA region provide new opportunities for growth. In 2018, we made additional investments in India to acquire full ownership of our express services unit, previously a joint venture. This follows the construction of a new facility in Hyderabad and an integrated logistics facility in Ahmedabad. These enhancements allow customers in ISMEA to reach markets in the U.S. and Europe within a 48-hour delivery window. In addition to these upgrades, we added Saturday delivery to seven countries in the region. The additional operating day gives our customers greater flexibility with their operations and scheduling.

## Supply Chain & Freight

Supply Chain & Freight consists of our forwarding, logistics, truckload brokerage, UPS Freight, UPS Capital and other businesses. Supply chain complexity creates demand for a global service offering that incorporates transportation, distribution and international trade and brokerage services, with complementary financial and information services. Outsourcing of non-core logistics activity is a strategy more companies are pursuing. With increased competition and growth opportunities in new markets, businesses require flexible and responsive supply chains to support their business strategies. We meet this demand by offering a broad array of supply chain services in more than 200 countries and territories.

### Forwarding

We are one of the largest U.S. domestic air freight carriers and among the top international air freight forwarders globally. We offer a portfolio of guaranteed and non-guaranteed global air freight services. Additionally, as one of the world's leading non-vessel operating common carriers, we provide ocean freight full-container load, less-than-container load and multimodal transportation services between most major ports around the world.

### Truckload Brokerage

Coyote Logistics Midco, Inc. ("Coyote"), a U.S.-based third party logistics provider, was acquired in August 2015. We successfully integrated this large-scale truckload brokerage and transportation management services operation into our Supply Chain & Freight segment and have seen significant synergies in the areas of purchased transportation,

backhaul utilization, technology systems and industry best practices. Coyote's access to our UPS fleet, combined with its broad carrier network, has created a customized capacity solution for all markets, customers and situations. Moreover, Coyote creates access to UPS services (such as air freight, customs brokerage and global freight forwarding) for its customer base.

Freightex, a U.K.- based freight brokerage firm, was acquired in January 2017. The acquisition of Freightex added a full-scale truckload brokerage and transportation management solution to UPS's European portfolio, creating a single-source solution for shippers throughout Europe with freight ranging from parcel to full truckload. In 2018, Freightex was rebranded to Coyote Logistics to further leverage the centralized technology and business models with the market knowledge, talent and established customer and carrier bases already in Europe. The Coyote Logistics European division complements UPS's North American truckload brokerage business, as many international shippers know and trust the Coyote truckload product.

## Logistics

We provide value-added fulfillment and transportation management services to customers through our global network of company-owned and leased distribution centers and field stocking locations. We leverage a global network of more than 900 facilities in more than 100 countries around the globe to ensure products and parts are in the right place, at the right time.

Our distribution centers are strategically located near UPS air and ground transportation hubs for rapid delivery to consumer and business markets. In 2017, UPS began piloting a new integrated transportation fulfillment solution for small business e-commerce merchants, enabling them to rapidly expand and grow their offerings without additional capital investments. In 2018, we expanded our network to support new business growth by adding more than 1.6 million square feet of distribution capacity.

Also in 2018, we rolled out new cloud-based transportation and warehouse management software platforms to drive higher operational efficiency and improve service to customers. The result has been better visibility, more rapid onboarding of customers and improved flexibility and response times.

Building on a 2017 pilot program, in 2018 we expanded a new integrated transportation-fulfillment solution for small business e-commerce merchants in the United States. The program enables small merchants to rapidly expand and grow their online offerings by providing connectivity to multiple marketplaces.

UPS Post Sales, our service parts logistics solution, relies on a global network of central and field stocking sites to provide critical spare parts when and where customers need them. In 2018, we implemented new technology to support our Implantable Medical Device solution, which helps ensure surgical kits and devices arrive safely and on time at hospitals and surgery centers. This integrated solution was built in collaboration with WebOps, a medical device logistics and analytics technology provider, and Baxter Planning, an inventory planning and optimization solutions provider. We continue to expand UPS Access Point locations into our network, offering greater flexibility, more convenience and improved service for our customers.

UPS Express Critical provides urgent, secure transportation for time-sensitive and high-value goods. It includes same-day, next-flight-out and door-to-door ground services, including specialized charter and hand-carry services for both lightweight and heavyweight shipments.

## UPS Freight

UPS Freight offers regional, inter-regional and long-haul less-than-truckload ("LTL") services in all 50 states, Canada, Puerto Rico, Guam, the U.S. Virgin Islands and Mexico. UPS Freight provides reliable LTL service backed by a day-definite, on-time guarantee at no additional cost. UPS Freight also provides dedicated contract carriage truckload services to select clients. Additionally, user friendly shipping, visibility and billing technology offerings, including UPS WorldShip, Quantum View and UPS Billing Center, allow freight customers to create electronic bills of lading, monitor shipment progress and reconcile shipping charges.

## Customs Brokerage

We are among the world's largest customs brokers by both the number of shipments processed annually and by the number of dedicated brokerage employees worldwide. In addition to customs clearance services, we also provide product classification, trade management, duty drawback and consulting services through STTAS, a UPS company. STTAS was acquired in 2017 and is a major differentiator in our ability to become the global broker of choice in all markets important to our customers. In 2017, we also added to our portfolio UPS Zone Solutions, a leader in Foreign Trade Zone administration services in the United States.

## UPS Capital

UPS Capital provides financial, insurance and payment services to leverage cash and help protect companies from risk in their supply chains. With services available in 22 countries and territories, UPS Capital and its affiliates support all aspects of the order-to-cash cycle, including financing inventory warehoused overseas, insuring shipments and providing payment solutions. The UPS Capital suite of insurance services, trade finance and payment solutions helps

customers protect their assets and keeps their businesses running smoothly. UPS Capital also offers insured transportation of high value goods including loose gemstones, finished jewelry and wristwatches.

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## Our People

The strength of our company is our people, working together with a common purpose. We had more than 481,000 employees (excluding temporary seasonal employees) as of December 31, 2018, of which 399,000 are in the U.S. and 82,000 are located internationally. Our global workforce includes approximately 85,000 management employees (41% of whom are part-time) and 396,000 hourly employees (50% of whom are part-time).

As of December 31, 2018, we had approximately 283,000 employees employed under a national master agreement and various supplemental agreements with local unions affiliated with the Teamsters. These agreements expired on July 31, 2018. On October 5, 2018, the Teamsters declared that the tentative national master agreement for the U.S. Domestic Package business unit was considered ratified, and will be implemented as soon as five remaining local and supplemental agreements are negotiated and ratified. We remain in the process of negotiating and ratifying four of these local and supplemental agreements which, when ratified, will be retroactive to August 1, 2018. The UPS Freight business unit national master agreement was ratified on November 11, 2018.

We have approximately 2,800 pilots who are employed under a collective bargaining agreement with the Independent Pilots Association ("IPA"), which becomes amendable on September 1, 2021.

Our airline mechanics are covered by a collective bargaining agreement with Teamsters Local 2727. On February 8, 2019, the airline mechanics who are covered by this agreement voted to ratify a new contract which will become amendable November 1, 2023. In addition, approximately 3,100 of our auto and maintenance mechanics who are not employed under agreements with the Teamsters are employed under collective bargaining agreements with the International Association of Machinists and Aerospace Workers ("IAM") that will expire on July 31, 2019.

## Competition

UPS is a global leader in logistics. We offer a broad array of services in the package and freight delivery industry and compete with many different local, regional, national and international logistics providers. Our competitors include worldwide postal services, various motor carriers, express companies, freight forwarders, air couriers and others, including startups that combine technology with crowdsourcing to focus on local market needs. Through our supply chain service offerings, we compete with a number of providers in the supply chain, financial services and information technology industries.

### Competitive Strengths

Our competitive strengths include:

**Global Network.** We believe that our integrated global ground and air network is the most extensive in the industry. We provide all types of package services (air, ground, domestic, international, commercial and residential) through a single pickup and delivery service network. We also have extensive air freight, ocean freight, ground freight and logistics networks that provide additional capabilities in the global transportation and logistics market. Our sophisticated engineering systems allow us to optimize our network efficiency and asset utilization on a daily basis.

**Global Presence.** We serve more than 220 countries and territories around the world. We have a significant presence in all of the world's major economies.

**Cutting-Edge Technology.** We are a global leader in developing technology that helps our customers enhance their shipping and logistics business processes to lower costs, improve service and increase efficiency.

Technology powers virtually every service we offer and every operation we perform. Customer need drives our technology offerings. We offer a variety of online service options that enable our customers to integrate UPS functionality into their own businesses not only to send, manage and track their shipments conveniently, but also to provide their customers with better information services. We provide the infrastructure for an internet presence that extends to tens of thousands of customers who have integrated UPS tools directly into their own websites.

**Broad Portfolio of Services.** Our portfolio of services helps customers choose the delivery option that is most appropriate for their requirements. Increasingly, our customers benefit from business solutions that integrate many

UPS services beyond package delivery. For example, our supply chain services – such as freight forwarding, truckload brokerage, customs brokerage, order fulfillment and returns management – help improve the efficiency of the supply chain management process.

**Customer Relationships.** We focus on building and maintaining long-term customer relationships. We serve 1.5 million shipping customers and more than 9.1 million delivery customers daily. Cross selling small package, supply chain and freight services across our customer base is an important growth mechanism for UPS.

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**Brand Equity.** We have built a leading and trusted brand that stands for quality service, reliability and service innovation. The distinctive appearance of our vehicles and the professional courtesy of our drivers are major contributors to our brand equity.

**Distinctive Culture.** We believe that the dedication of our employees comes in large part from our distinctive “employee-owner” concept. Our employee stock ownership tradition dates back to 1927, when our founders, who believed that employee stock ownership was a vital foundation for successful business, first offered stock to employees. To encourage employee stock ownership, we maintain several stock-based compensation programs.

**Financial Strength.** Our financial strength gives us the resources to achieve global scale; to invest in employee development, technology, transportation equipment and facilities; to pursue strategic opportunities that facilitate our growth; to service our obligations and to return value to our shareowners in the form of dividends, share repurchases and steady share growth.

#### Government Regulation

We are subject to numerous laws and regulations in connection with our package and non-package businesses in the countries in which we operate. Certain of these laws and regulations are summarized below.

#### Air Operations

The U.S. Department of Transportation (“DOT”), the Federal Aviation Administration (“FAA”) and the U.S. Department of Homeland Security, through the Transportation Security Administration (“TSA”), have regulatory authority over United Parcel Service Co.’s (“UPS Airlines”) air transportation services. The Federal Aviation Act of 1958, as amended, is the statutory basis for DOT and FAA authority and the Aviation and Transportation Security Act of 2001, as amended, is the basis for TSA aviation security authority.

The DOT’s authority primarily relates to economic aspects of air transportation, such as insurance requirements, discriminatory pricing, non-competitive practices, interlocking relations and cooperative agreements. The DOT also regulates, subject to the authority of the President of the United States, international routes, fares, rates and practices and is authorized to investigate and take action against discriminatory treatment of U.S. air carriers abroad.

International operating rights for U.S. airlines are usually subject to bilateral agreements between the U.S. and foreign governments or, in the absence of such agreements, by principles of reciprocity. We are also subject to current and potential aviation regulations imposed by foreign governments in the countries in which we operate, including registration and license requirements and security regulations. UPS Airlines has international route operating rights granted by the DOT and we may apply for additional authorities when those operating rights are available and are required for the efficient operation of our international network. The efficiency and flexibility of our international air transportation network is dependent on DOT and foreign government regulations and operating restrictions.

The FAA’s authority primarily relates to safety aspects of air transportation, including aircraft operating procedures, transportation of hazardous materials, record keeping standards and maintenance activities and personnel. In 1988, the FAA granted us an operating certificate, which remains in effect so long as we meet the safety and operational requirements of the applicable FAA regulations. In addition, we are subject to non-U.S. government regulation of aviation rights involving non-U.S. jurisdictions and non-U.S. customs regulation.

UPS aircraft maintenance programs and procedures, including aircraft inspection and repair at periodic intervals, are approved for all aircraft under FAA regulations. The future cost of repairs pursuant to these programs may fluctuate according to aircraft condition, age and the enactment of additional FAA regulatory requirements.

The TSA regulates various security aspects of air cargo transportation in a manner consistent with the TSA mission statement to “protect the Nation’s transportation systems to ensure freedom of movement for people and commerce.” UPS Airlines, and specified airport and off-airport locations, are regulated under TSA regulations applicable to the transportation of cargo in an air network. In addition, personnel, facilities and procedures involved in air cargo transportation must comply with TSA regulations.

UPS Airlines, along with a number of other domestic airlines, participates in the Civil Reserve Air Fleet (“CRAF”) program. Our participation in the CRAF program allows the U.S. Department of Defense (“DOD”) to requisition specified UPS Airlines aircraft for military use during a national defense emergency. The DOD is required to compensate us for the use of aircraft under the CRAF program. In addition, participation in CRAF entitles UPS Airlines to bid for other U.S. Government opportunities including small package and air freight.

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### Ground Operations

Our ground transportation of packages in the U.S. is subject to regulation by the DOT and its agency, the Federal Motor Carrier Safety Administration (the “FMCSA”) and the states’ jurisdiction with respect to the regulation of operations, safety, insurance and hazardous materials. We also must comply with the safety and fitness regulations promulgated by the FMCSA, including those relating to drug and alcohol testing and hours of service for drivers. We are subject to similar regulation in many non-U.S. jurisdictions.

The Postal Reorganization Act of 1970 created the U.S. Postal Service as an independent establishment of the executive branch of the federal government, and created the Postal Rate Commission, an independent agency, to recommend postal rates. The Postal Accountability and Enhancement Act of 2006 amended the 1970 Act to give the re-named Postal Regulatory Commission revised oversight authority over many aspects of the Postal Service, including postal rates, product offerings and service standards. We sometimes participate in the proceedings before the Postal Regulatory Commission in an attempt to secure fair postal rates for competitive services.

Our ground operations are subject to compliance with various cargo-security and transportation regulations issued by the U.S. Department of Homeland Security, including regulation by the TSA.

### Customs

We are subject to the customs laws in the countries in which we operate, regarding the import and export of shipments, including those related to the filing of documents on behalf of client importers and exporters. Our activities in the U.S., including customs brokerage and freight forwarding, are subject to regulation by the Bureau of Customs and Border Protection, the TSA, the U.S. Federal Maritime Commission and the DOT. Our international operations are subject to similar regulatory structures in their respective jurisdictions.

### Environmental

We are subject to federal, state and local environmental laws and regulations across all of our business units. These laws and regulations cover a variety of processes, including, but not limited to: proper storage, handling and disposal of waste materials; appropriately managing wastewater and stormwater; monitoring and maintaining the integrity of underground storage tanks; complying with laws regarding clean air, including those governing emissions; protecting against and appropriately responding to spills and releases and communicating the presence of reportable quantities of hazardous materials to local responders. We have established site- and activity-specific environmental compliance and pollution prevention programs to address our environmental responsibilities and remain compliant. In addition, we have created numerous programs which seek to minimize waste and prevent pollution within our operations.

Pursuant to the Federal Aviation Act, the FAA, with the assistance of the Environmental Protection Agency (“EPA”), is authorized to establish standards governing aircraft noise. Our aircraft fleet is in compliance with current noise standards of the federal aviation regulations. Our international operations are also subject to noise regulations in certain countries in which we operate.

### Communications and Data Protection

Because of our extensive use of radio and other communication facilities in our aircraft and ground transportation operations, we are subject to the Federal Communications Act of 1934, as amended. In addition, the Federal Communications Commission regulates and licenses our activities pertaining to satellite communications. There has recently been increased regulatory and enforcement focus on data protection in the U.S. (at both the state and federal level) and in other countries. For example, the European Union (“E.U.”) General Data Protection Regulation (“GDPR”), which became effective in May 2018, greatly increases the jurisdictional reach of E.U. law and increases the requirements related to personal data, including individual notice and opt-out preferences and public disclosure of significant data breaches. Additionally, violations of the GDPR can result in significant fines. Other governments have enacted or are enacting similar data protection laws, and are considering data localization laws that would govern the use of data outside of their respective jurisdictions.

### Where You Can Find More Information

We maintain a website at [www.ups.com](http://www.ups.com). Our annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and any amendments to those reports filed with or furnished to the SEC pursuant to Section 13(a) of the Securities Exchange Act of 1934 are made available through our website [www.investors.ups.com](http://www.investors.ups.com) as soon as reasonably practical after we electronically file or furnish the reports to the SEC. However, information on these websites is not incorporated by reference into this report or any other report filed with or furnished to the SEC.

We have adopted a written Code of Business Conduct that applies to all of our directors, officers and employees, including our principal executive officer and senior financial officers. It is available in the governance section of our investor relations website, located at [www.investors.ups.com](http://www.investors.ups.com). In the event that we make changes in, or provide waivers from, the provisions of the Code of Business Conduct that the SEC requires us to disclose, we intend to disclose these events in the governance section of our investor relations website.

Our Corporate Governance Guidelines and the Charters for our Audit Committee, Compensation Committee, Executive Committee, Risk Committee and Nominating and Corporate Governance Committee are also available in the governance section of our investor relations website.

Our sustainability report, which describes our activities that support our commitment to acting responsibly and contributing to society, is available at [www.sustainability.ups.com](http://www.sustainability.ups.com). We provide the addresses to our internet sites solely for the information of investors. We do not intend for any addresses to be active links or to otherwise incorporate the contents of any website into this report.

## Item 1A. Risk Factors

Our business, financial condition and results are subject to numerous risks and uncertainties. In connection with any investment decision, you should carefully consider the following factors, which could materially affect our business, financial condition or results of operations. You should read these Risk Factors in conjunction with “Management’s Discussion and Analysis of Financial Condition and Results of Operations” in Item 7 and our Consolidated Financial Statements and related notes in Item 8.

General economic conditions, both in the U.S. and internationally, may adversely affect our results of operations. We conduct operations in over 220 countries and territories. Our U.S. and international operations are subject to normal cycles affecting the economy in general, as well as the local economic environments in which we operate. The factors that create cyclical changes to the economy and to our business are beyond our control, may adversely impact our credit rating and it may be difficult for us to adjust our business model to mitigate the impact of these factors. In particular, our business is affected by levels of industrial production, consumer spending and retail activity and our business, financial position and results of operations could be materially affected by adverse developments in these aspects of the economy. In addition, there remains substantial economic uncertainty arising from the United Kingdom’s 2016 vote to leave the European Union. In 2017 the U.K. government initiated a process to leave the E.U., and the U.K. and the E.U. continue to negotiate the future relationship between the U.K. and the E.U., which could take several years to finalize. The results of these negotiations could result in, among other things, fewer goods being transported globally, volatility in currency exchange rates and further regulations relating to, among other things, trade and aviation. Any of the foregoing could materially adversely affect our business, financial position and results of operations.

We face significant competition which could adversely affect our business, financial position and results of operations.

We face significant competition on a local, regional, national and international basis. Our competitors include the postal services of the U.S. and other nations, various motor carriers, express companies, freight forwarders, air couriers and others, including start ups and other companies that combine technologies with crowdsourcing to focus on local market needs. Competition may also come from other sources in the future, including as a result of the development of new technologies. Some of our competitors may have cost and organizational structures that differ from ours and may offer services and pricing terms that we may not be willing or able to offer. Additionally, to remain competitive, we may have to raise costs to our customers and our customers may not be willing to accept these higher costs. If we are unable to timely and appropriately respond to competitive pressures, our business, financial position and results of operations could be adversely affected.

The transportation industry continues to consolidate and competition remains strong. As a result of consolidation, our competitors may increase their market share and improve their financial capacity, and may strengthen their competitive positions. Business combinations could also result in competitors providing a wider variety of services and products at competitive prices, which could adversely affect our financial performance.

Changes in our relationships with our significant customers, including the loss or reduction in business from one or more of them, could have an adverse impact on us.

No single customer accounts for 10% or more of our consolidated revenue. We do not believe the loss of any single customer would materially impair our overall financial condition or results of operations; however, collectively, some of our large customers might account for a relatively significant portion of the growth in revenue in a particular quarter or year. These customers can drive the growth in revenue for particular services based on factors such as: new customer product launches; trends in the e-commerce industry, such as the seasonality associated with the fourth quarter holiday season; business mergers and acquisitions and the overall fast growth of a customer's underlying business. These customers could choose to divert all or a portion of their business with us to one of our competitors,

demand pricing concessions for our services, require us to provide enhanced services that increase our costs, or develop their own shipping and distribution capabilities. If these factors drove some of our large customers to cancel all or a portion of their business relationships with us, it could materially impact the growth in our business and the ability to meet our current and long-term financial forecasts.

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Our business is subject to complex and stringent regulation in the U.S. and internationally, which could increase our operating costs.

We are subject to complex and stringent aviation, transportation, environmental, security, labor, employment and other governmental laws, regulations and policies, both in the U.S. and in the other countries in which we operate. In addition, our business is impacted by laws, regulations and policies that affect global trade, including tariff and trade policies, export requirements, taxes, monetary policies and other restrictions and charges. Recently, trade discussions between the U.S. and some of its trading partners have been fluid, and any trade agreements that may be entered into are subject to a number of uncertainties, including the imposition of new tariffs or adjustments and changes to the products covered by existing tariffs. The impact of new laws, regulations and policies cannot be predicted. Compliance with new laws and regulations may increase our operating costs or require significant capital expenditures. Any failure to comply with applicable laws or regulations in the U.S. or in any of the countries in which we operate could result in substantial fines or possible revocation of our authority to conduct our operations, which could adversely affect our financial performance.

Increased security requirements could impose substantial costs on us and we could be the target of an attack or have a security breach.

As a result of concerns about global terrorism and homeland security, governments around the world have adopted or may adopt stricter security requirements that will result in increased operating costs for businesses in the transportation industry. These requirements may change periodically as a result of regulatory and legislative requirements and in response to evolving threats. We cannot determine the effect that these new requirements will have on our cost structure or our operating results, and these rules or other future security requirements may increase our costs of operations and reduce operating efficiencies. Regardless of our compliance with security requirements or the steps we take to secure our facilities or fleet, we could be the target of an attack or security breaches could occur, which could materially adversely affect our operations or our reputation.

We are subject to increasingly stringent regulations related to climate change, and new regulations could materially increase our operating costs.

Concern over climate change, including the impact of global warming, has led to significant legislative and regulatory efforts, particularly internationally but also in the United States, to limit greenhouse gas (“GHG”) emissions. State and local governments also are increasingly considering GHG regulation. The possibility of increased regulation of GHG emissions potentially exposes our transportation and logistics businesses to significant new taxes, fees and other costs. Compliance with such potential regulation or the associated potential costs is further complicated by the fact that various countries and regions are following different approaches to the regulation of climate change.

For example, in 2009 the European Commission approved the extension to the airline industry of the European Union Emissions Trading Scheme (“ETS”) for GHG emissions. Under this decision, all of our flights operating within the European Union are covered by the ETS requirements, and we are required annually to purchase emission allowances in an amount exceeding the number of free allowances allocated to us under the ETS. Similarly, in 2016, the International Civil Aviation Organization (“ICAO”) passed a resolution adopting the Carbon Offsetting and Reduction Scheme for International Aviation (“CORSIA”), which is a global, market-based emissions offset program to encourage carbon-neutral growth beyond 2020. A pilot phase is scheduled to begin in 2021 in which countries may voluntarily participate, and full mandatory participation is scheduled to begin in 2027. ICAO continues to develop details regarding implementation, but compliance with CORSIA will increase our operating costs.

In the U.S., Congress in the past several years has considered various bills that would regulate GHG emissions, but these bills so far have not received sufficient Congressional support for enactment. Nevertheless, some form of federal climate change legislation is possible in the future. Even in the absence of such legislation, the Environmental Protection Agency (“EPA”), spurred by judicial interpretation of the Clean Air Act, could determine to regulate GHG



emissions, especially aircraft or diesel engine emissions, and this could impose substantial costs on us. In August 2017, the U.S. announced its intention to withdraw from the Paris climate accord, an agreement among 196 countries to reduce GHG emissions, and the effect of that withdrawal on future U.S. policy regarding GHG emissions, on CORSIA and on other GHG regulation is uncertain. Nevertheless, the extent to which other countries implement that agreement could have an adverse direct or indirect effect on our business.

We may face additional regulations regarding GHG emissions internationally and in the United States. Potential costs to us of increased regulation regarding GHG emissions, especially aircraft or diesel engine emissions, include an increase in the cost of the fuel and other energy we purchase and capital costs associated with updating or replacing our aircraft or vehicles prematurely. We cannot predict the impact any future regulation would have on our cost structure or our operating results. It is possible that such regulation could significantly increase our operating expenses if we are unable to pass such costs along to our customers. Moreover, even without such regulation, increased awareness and any adverse publicity in the global marketplace about the GHGs emitted by companies in the airline and transportation industries could harm our reputation and reduce customer demand for our services, especially our air services.

Strikes, work stoppages and slowdowns by our employees could adversely affect our business, financial position and results of operations.

A significant number of our employees are employed under a national master agreement and various supplemental agreements with local unions affiliated with the Teamsters. In addition, our airline pilots, airline mechanics, ground mechanics and certain other employees are employed under other collective bargaining agreements. Strikes, work stoppages and slowdowns by our employees could adversely affect our ability to meet our customers' needs, and customers may do more business with competitors if they believe that such actions or threatened actions may adversely affect our ability to provide services. We may face a permanent loss of customers if we are unable to provide uninterrupted service, and this could materially adversely affect our business, financial position and results of operations. The terms of future collective bargaining agreements also may affect our competitive position and results of operations.

We are exposed to the effects of changing prices of energy, as well as gasoline, diesel and jet fuel, and interruptions in supplies of these commodities.

Changing fuel and energy costs may have a significant impact on our operations. We require significant quantities of fuel for our aircraft and delivery vehicles and are exposed to the risk associated with variations in the market price for petroleum products, including gasoline, diesel and jet fuel. We mitigate our exposure to changing fuel prices through our indexed fuel surcharges and we may also enter into hedging transactions from time to time. If we are unable to maintain or increase our fuel surcharges, higher fuel costs could adversely impact our operating results. Even if we are able to offset the cost of fuel with our surcharges, high fuel surcharges may result in a mix shift from our higher-yielding air products to lower-yielding ground products or an overall reduction in volume. There can be no assurance that our hedging transactions will be effective to protect us from changes in fuel prices. Moreover, we could experience a disruption in energy supplies as a result of war, actions by producers or other factors beyond our control, which could have a material adverse effect on our business.

Changes in exchange rates or interest rates may have a material adverse effect on our results.

We conduct business across the globe with a significant portion of our revenue derived from operations outside the United States. Our operations in international markets are affected by changes in the exchange rates for local currencies, and in particular the Euro, British Pound Sterling, Canadian Dollar, Chinese Renminbi and Hong Kong Dollar.

We are exposed to changes in interest rates, primarily on our short-term debt and that portion of our long-term debt that carries floating interest rates. The impact of a 100-basis-point change in interest rates affecting our debt is discussed in the "Quantitative and Qualitative Disclosures about Market Risk" section of this report. Additionally, changes in interest rates impact the valuation of our pension and postretirement benefit obligations and the related benefit cost recognized in the income statement. The impact of changes in interest rates on our pension and postretirement benefit obligations and costs is discussed further in the "Critical Accounting Policies and Estimates" section of this report.

We monitor and manage our exposures to changes in currency exchange rates and interest rates, and make use of derivative instruments to mitigate the impact of changes in these rates on our financial position and results of operations; however, changes in exchange rates and interest rates cannot always be predicted or hedged.

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If we are unable to maintain our brand image and corporate reputation, our business may suffer.

Our success depends in part on our ability to maintain the image of the UPS brand and our reputation for providing excellent service to our customers. Service quality issues, actual or perceived, even when false or unfounded, could tarnish the image of our brand and may cause customers to use other companies. Also, adverse publicity surrounding labor relations, environmental concerns, security matters, political activities and the like, or attempts to connect our company to these sorts of issues, either in the United States or other countries in which we operate, could negatively affect our overall reputation and acceptance of our services by customers. Social media may accelerate and amplify the scope of negative publicity, and increase the challenge of responding to negative claims. Damage to our reputation and loss of brand equity could reduce demand for our services and thus have a material adverse effect on our business, financial position and results of operations, and could require additional resources to rebuild our reputation and restore the value of our brand.

A significant data breach or IT system disruption could adversely affect our business, financial results, or reputation, and we may be required to increase our spending on data and system security.

We rely heavily on information technology networks and systems, including the Internet, to manage or support a wide variety of important business processes and activities throughout our operations. For example, we rely on information technology to receive package level information in advance of physical receipt of packages, to track items that move through our delivery systems, to efficiently plan deliveries, to execute billing processes, and to track and report financial and operational data. Our franchised center locations and businesses we have acquired also are reliant on the use of information technology systems to manage their business processes and activities.

In addition, the provision of service to our customers and the operation of our networks and systems involve the storage and transmission of significant amounts of proprietary information and sensitive or confidential data, including personal information of customers, employees and others. To conduct our operations, we regularly move data across national borders, and consequently we are subject to a variety of continuously evolving and developing laws and regulations in the United States and abroad regarding privacy, data protection and data security. The scope of the laws that may be applicable to us is often uncertain and may be conflicting, particularly with respect to foreign laws. For example, the European Union's General Data Protection Regulation ("GDPR"), which greatly increases the jurisdictional reach of European Union law and adds a broad array of requirements for handling personal data, including the public disclosure of significant data breaches, became effective in May 2018. Other countries have enacted or are enacting data localization laws that require data to stay within their borders. All of these evolving compliance and operational requirements impose significant costs that are likely to increase over time.

Our information technology systems (as well as those of our franchisees and acquired businesses) may be susceptible to damage, disruptions or shutdowns due to failures during the process of upgrading or replacing software, databases or components thereof, power outages, hardware failures, computer viruses, cyber-attacks, ransomware attacks, malware attacks, malicious employees or other insiders, telecommunications failures, human errors or catastrophic events. Hackers, foreign governments, cyber-terrorists and cyber-criminals, acting individually or in coordinated groups, may launch distributed denial of service attacks or other coordinated attacks that may cause service outages, gain inappropriate or block legitimate access to systems or information, or result in other interruptions in our business. In addition, breaches in security could expose us, our customers and franchisees, or the individuals affected, to a risk of loss or misuse of proprietary information and sensitive or confidential data, including personal information of customers, employees and others. The techniques used to obtain unauthorized access, disable or degrade service or sabotage systems change frequently, may be difficult to detect for a long time and often are not recognized until launched against a target. As a result, we may be unable to anticipate these techniques or to implement adequate preventative measures.

We also depend on and interact with the information technology networks and systems of third-parties for many aspects of our business operations, including our customers and franchisees and service providers such as cloud

service providers and third-party delivery services. These third parties may have access to information we maintain about our company, operations, customers, employees and vendors, or operating systems that are critical to or can significantly impact our business operations. Like us, these third-parties are subject to risks imposed by data breaches and cyber-attacks and other events or actions that could damage, disrupt or close down their networks or systems. Security processes, protocols and standards that we have implemented and contractual provisions requiring security measures that we may have sought to impose on such third-parties may not be sufficient or effective at preventing such events, which could result in unauthorized access to, or disruptions or denials of access to, or misuse of, information or systems that are important to our business, including proprietary information, sensitive or confidential data, and other information about our operations, customers, employees and suppliers, including personal information.

Any of these events that impact our information technology networks or systems, or those of acquired businesses, franchisees, customers, service providers or other third-parties, could result in disruptions in our operations, the loss of existing or potential customers, damage to our brand and reputation, regulatory scrutiny, and litigation and potential liability for us. Among other consequences, our customers' confidence in our ability to protect data and systems and to provide services consistent with their expectations could be impacted, further disrupting our operations. Similarly, an actual or alleged failure to comply with applicable U.S. or foreign data protection regulations or other data protection standards may expose us to litigation, fines, sanctions or other penalties.

We have invested and continue to invest in technology security initiatives, information technology risk management and disaster recovery plans. The cost and operational consequences of implementing, maintaining and enhancing further data or system protection measures could increase significantly to overcome increasingly intense, complex and sophisticated global cyber threats. Despite our best efforts, we are not fully insulated from data breaches and system disruptions. For example, in 2014, a broad-based malware intrusion targeting retailers throughout the U.S. was discovered and subsequently eradicated at approximately 1% of our franchisees' locations. While the impact of this cyber-attack, including the costs associated with investigation and remediation activities, was not material to our business and our financial results, there is no assurance that such impacts will not be material in the future, and our efforts to deter, identify, mitigate and/or eliminate future breaches may require significant additional effort and expense and may not be successful.

Severe weather or other natural or manmade disasters could adversely affect our business.

Severe weather conditions and other natural or manmade disasters, including storms, floods, fires or earthquakes, epidemics or pandemics, conflicts or unrest, or terrorist attacks, may result in decreased revenues, as our customers reduce their shipments, or increased costs to operate our business, which could have a material adverse effect on our results of operations for a quarter or year. Any such event affecting one of our major facilities could result in a significant interruption in or disruption of our business.

We make significant capital investments in our business of which a significant portion is tied to projected volume levels.

We require significant capital investments in our business consisting of aircraft, vehicles, technology, facilities and sorting and other types of equipment to support both our existing business and anticipated growth. Forecasting projected volume involves many factors which are subject to uncertainty, such as general economic trends, changes in governmental regulation and competition. If we do not accurately forecast our future capital investment needs, we could have excess capacity or insufficient capacity, either of which would negatively affect our revenues and profitability. In addition to forecasting our capital investment requirements, we adjust other elements of our operations and cost structure in response to adverse economic conditions; however, these adjustments may not be sufficient to allow us to maintain our operating margins in a weak economy.

We derive a significant portion of our revenues from our international operations and are subject to the risks of doing business in international markets.

We have significant international operations, and while the geographical diversity of our international operations helps ensure that we are not overly reliant on a single region or country, we are continually exposed to changing economic, political and social developments that are beyond our control. Emerging markets are typically more volatile than those in the developed world, and any broad-based downturn in these markets could reduce our revenues and adversely affect our business, financial position and results of operations. We are subject to many laws governing our international operations, including those that prohibit improper payments to government officials and commercial customers, and restrict where we can do business, our shipments to certain countries and the information that we can provide to non-U.S. governments.

We are subject to changes in markets and our business plans that have resulted, and may in the future result, in substantial write-downs of the carrying value of our assets, thereby reducing our net income.

Our regular review of the carrying value of our assets has resulted, from time to time, in significant impairments, and we may in the future be required to recognize additional impairment charges. Changes in business strategy, government regulations, or economic or market conditions have resulted and may result in further substantial impairments of our intangible, fixed or other assets at any time in the future. In addition, we have been and may be required in the future to recognize increased depreciation and amortization charges if we determine that the useful lives of our fixed assets or intangible assets are shorter than we originally estimated. Such changes could reduce our net income.

Employee health and retiree health and pension benefit costs represent a significant expense to us; further cost increases could materially and adversely affect us.

Our expenses relating to employee health and retiree health and pension benefits are significant. In recent years, we have experienced significant increases in some of these costs, largely as a result of economic factors beyond our control, including, in particular, ongoing increases in healthcare costs well in excess of the rate of inflation and historically low discount rates that we use to value our benefit plan obligations. Continually increasing healthcare costs, volatility in investment returns and discount rates, as well as changes in laws, regulations and assumptions used to calculate retiree health and pension benefit expenses, may adversely affect our business, financial position, results of operations or require significant contributions to our benefit plans. Our national master agreement with the Teamsters includes provisions that are designed to mitigate certain of these healthcare expenses, but there can be no assurance that our efforts will be successful or that the failure or success of these efforts will not materially adversely affect our business, financial position, results of operations or liquidity.

We participate in a number of trustee-managed multiemployer pension and health and welfare plans for employees covered under collective bargaining agreements. As part of the overall collective bargaining process for wage and benefit levels, we have agreed to contribute certain amounts to the multiemployer benefit plans during the contract period. The multiemployer benefit plans set benefit levels and are responsible for benefit delivery to participants. Future contribution amounts to multiemployer benefit plans will be determined only through collective bargaining, and we have no additional legal or constructive obligation to increase contributions beyond the agreed-upon amounts. However, in future collective bargaining negotiations, we could agree to make significantly higher future contributions to improve the funded status of one or more of these plans. The funded status of these multiemployer plans is impacted by various factors, including investment performance, healthcare inflation, changes in demographics and changes in participant benefit levels. At this time, we are unable to determine the amount of additional future contributions, if any, or whether any material adverse effect on our financial condition, results of operations or liquidity could result from our participation in these plans.

In addition to our on-going multiemployer pension plan obligations, we may have additional exposure with respect to benefits earned in the Central States Pension Fund (the "CSPF"). UPS was a contributing employer to the CSPF until 2007 when we withdrew from the CSPF and fully funded our allocable share of unfunded vested benefits by paying a \$6.1 billion withdrawal liability. Under a collective bargaining agreement with the International Brotherhood of Teamsters ("IBT"), UPS agreed to provide coordinating benefits in the UPS/IBT Full Time Employee Pension Plan ("UPS/IBT Plan") for UPS participants whose last employer was UPS and who had not retired as of January 1, 2008 ("the UPS Transfer Group") in the event that benefits are lawfully reduced by the CSPF in the future consistent with the terms of our withdrawal agreement with the CSPF. Under our withdrawal agreement with the CSPF, benefits to the UPS Transfer Group cannot be reduced without our consent and can only be reduced in accordance with applicable law.

In December 2014, Congress passed the Multiemployer Pension Reform Act ("MPRA"). This change in law for the first time permitted multiemployer pension plans to reduce benefit payments to retirees, subject to specific guidelines in the statute and government approval. In September 2015, the CSPF submitted a proposed pension benefit reduction plan to the U.S. Department of the Treasury ("Treasury"). In May 2016, Treasury rejected the proposed plan submitted by the CSPF. In the first quarter of 2018, Congress established a Joint Select Committee to develop a recommendation to improve the solvency of multiemployer plans and the Pension Benefit Guaranty Corporation ("PBGC") before a November 30, 2018 deadline. While the Committee's efforts failed to meet its deadline, the Committee made significant progress towards finding solutions that will address the long term solvency of multiemployer pension plans. UPS will continue to work with all stakeholders, including legislators and regulators, to implement an acceptable solution.



The CSPF has said that it believes a legislative solution to its funded status is necessary or that it will become insolvent in 2025, and we expect that the CSPF will continue to explore options to avoid insolvency. Numerous factors could affect the CSPF's funded status and UPS's potential obligation to pay coordinating benefits under the UPS/IBT Plan. Any obligation to pay coordinating benefits will be subject to a number of significant uncertainties, including whether the CSPF submits a revised MPRA filing and the terms thereof, or whether it otherwise seeks federal government assistance, as well as the terms of any applicable legislation, the extent to which benefits are paid by the PBGC and our ability to successfully defend legal positions we may take in the future under the MPRA, including the suspension ordering provisions, our withdrawal agreement and other applicable law.

We account for the potential obligation to pay coordinating benefits to the UPS Transfer Group under Accounting Standards Codification Topic 715- Compensation- Retirement Benefits ("ASC 715"), which requires us to provide a best estimate of various actuarial assumptions, including the eventual outcome of this matter, in measuring our pension benefit obligation at the December 31st measurement date. While we currently believe the most likely outcome to this matter and the broader systemic problems facing multiemployer pension plans is intervention by the federal government, ASC 715 does not permit anticipation of changes in law in making a best estimate of pension liabilities.

As such, our best estimate of the next most likely outcome at the measurement date is that the CSPF submits and implements another benefit reduction plan under the MPRA during 2019. We believe any MPRA filing would be designed to forestall insolvency by reducing benefits to participants other than the UPS Transfer Group to the maximum extent permitted, and then reducing benefits to the UPS Transfer Group by a lesser amount.

We have evaluated this outcome using a deterministic cash flow projection, reflecting updated estimated CSPF cash flows and investment earnings, the lack of legislative action and the absence of a MPRA filing by the CSPF in 2018. As a result, at the December 31, 2018 measurement date, the best estimate of our projected benefit obligation increased by \$1.6 billion for coordinating benefits that may be required to be directly provided by the UPS/IBT Plan to the UPS Transfer Group.

The future value of this estimate will be influenced by the terms and timing of any MPRA filing, changes in our discount rate, rate of return on assets and other actuarial assumptions, presumed solvency of the PBGC, as well as potential solutions resulting from federal government intervention. Any such event may result in a decrease or an increase in the best estimate of our projected benefit obligation. If the uncertainties are not resolved, it is reasonably possible that our projected benefit obligation could increase by approximately \$2.4 billion, resulting in a total obligation for coordinating benefits of approximately \$4.0 billion as previously disclosed. If a future change in law occurs, it may be a significant event requiring an interim remeasurement of the UPS/IBT Plan at the date the law is enacted. We will continue to assess the impact of these uncertainties on our projected benefit obligation in accordance with ASC 715.

We may have additional tax liabilities.

We are subject to income taxes in the U.S. and many foreign jurisdictions. Significant judgment is required in determining our worldwide provision for income taxes. In the course of our business, there are many transactions and calculations where the ultimate tax determination is uncertain. For example, compliance with the 2017 United States Tax Cuts and Jobs Act (the "Tax Act") may require the collection of information not regularly produced within our company and the exercise of significant judgment in accounting for its provisions. Many aspects of the Tax Act remain unclear and may not be clarified for some time. In addition, many state jurisdictions continue to issue guidance on the state treatment of certain aspects of the Tax Act. As regulations and guidance evolve with respect to the Tax Act, our results may differ from previous estimates and may materially affect our tax rates and our financial position. We regularly are under audit by tax authorities in different jurisdictions. Economic and political pressures to increase tax revenue in various jurisdictions may make resolving tax disputes favorably more difficult. Although we believe our tax estimates are reasonable, the final determination of tax audits and any related litigation in the jurisdictions where we are subject to taxation could be materially different from our historical income tax provisions and accruals. In addition, changes in U.S. federal and state or international tax laws applicable to corporate multinationals, other fundamental law changes currently being considered by many countries, including the U.S., and changes in taxing jurisdictions' administrative interpretations, decisions, policies and positions may materially adversely impact our tax expense and cash flows.

We may be subject to various claims and lawsuits that could result in significant expenditures.

The nature of our business exposes us to the potential for various claims and litigation related to labor and employment, personal injury, property damage, business practices, environmental liability and other matters. Any material litigation or a catastrophic accident or series of accidents could have a material adverse effect on our business, financial position and results of operations.

We may not realize the anticipated benefits of acquisitions, joint ventures or strategic alliances.

As part of our business strategy, we may acquire businesses and form joint ventures or strategic alliances. Whether we realize the anticipated benefits from these transactions depends, in part, upon the successful integration between the businesses involved, the performance of the underlying operations, capabilities or technologies and the management of the acquired operations. Accordingly, our financial results could be materially adversely affected by our failure to

effectively integrate the acquired operations, unanticipated performance issues, transaction-related charges or charges for impairment of long-term assets that we acquire.

Insurance and claims expenses could have a material adverse effect on our business, financial condition and results of operations.

We have a combination of both self-insurance and high-deductible insurance programs for the risks arising out of the services we provide and the nature of our global operations, including claims exposure resulting from cargo loss, personal injury, property damage, aircraft and related liabilities, business interruption and workers' compensation. Workers' compensation, automobile and general liabilities are determined using actuarial estimates of the aggregate liability for claims incurred and an estimate of incurred but not reported claims, on an undiscounted basis. Our accruals for insurance reserves reflect certain actuarial assumptions and management judgments, which are subject to a high degree of variability. If the number or severity of claims for which we are retaining risk increases, our financial condition and results of operations could be adversely affected. If we lose our ability to self-insure these risks, our insurance costs could materially increase and we may find it difficult to obtain adequate levels of insurance coverage.

Item 1B. Unresolved Staff Comments

Not applicable.

Item 2. Properties

Operating Facilities

We own our headquarters, which is located in Atlanta, Georgia and consists of about 745,000 square feet of office space in an office campus, and our UPS Supply Chain Solutions group's headquarters, which is located in Alpharetta, Georgia and consists of about 310,000 square feet of office space.

We own or lease over 1,000 package operating facilities in the U.S., with approximately 73 million square feet of floor space. The smaller of these facilities have vehicles and drivers stationed for the pick-up and delivery of packages, and capacity to sort and transfer packages. The larger of these facilities also service our vehicles and equipment, and employ specialized mechanical installations for the sorting and handling of packages. We own or lease approximately 800 facilities that support our international package operations, with approximately 22 million square feet of floor space.

In addition, we own or lease more than 500 facilities, with approximately 35 million square feet of floor space, that support our freight forwarding and logistics operations. We own and operate a logistics campus consisting of approximately 4 million square feet in Louisville, Kentucky.

We own or lease approximately 200 UPS Freight service centers with approximately 6 million square feet of floor space. The main offices of UPS Freight are located in Richmond, Virginia and consist of about 217,000 square feet of office space.

Our aircraft are operated in a hub and spoke pattern in the U.S., with our principal air hub, known as Worldport, located in Louisville, Kentucky. The Worldport facility consists of over 5 million square feet and includes high-speed conveyor and computer control systems.

We also own or lease regional air hubs globally, with over 4 million square feet of floor space. Our U.S. regional air hubs are located in Dallas, Texas; Ontario, California; Philadelphia, Pennsylvania; and Rockford, Illinois. These hubs house facilities for the sorting, transfer and delivery of packages. Our European air hub is located in Cologne, Germany, and we maintain Asia-Pacific air hubs in Shanghai, China; Shenzhen, China; and Hong Kong. Our regional air hub in Canada is located in Hamilton, Ontario, and our regional air hub for Latin America and the Caribbean is in Miami, Florida.

Our primary information technology operations are consolidated in a 444,000 square foot owned facility, the Ramapo Ridge facility, in Mahwah, New Jersey. Our information technology headquarters is located in Parsippany, New Jersey, consisting of about 200,000 square feet of office space. We also own a 175,000 square foot facility in Alpharetta, Georgia, which serves as a backup to the main information technology operations facility in New Jersey. This facility provides production functions and backup capacity in the event that a power outage or other disaster incapacitates the main data center. It also helps to meet our internal communication needs.

## Fleet

## Aircraft

The following table shows information about our aircraft fleet as of December 31, 2018:

Description	Owned and Capital Leases	Short-term		
		Leased or Chartered From Others	On Order	Under Option
Boeing 757-200	75	—	—	—
Boeing 767-200	—	2	—	—
Boeing 767-300	59	—	9	—
Boeing 767-300BCF 3	—	—	—	—
Airbus A300-600	52	—	—	—
Boeing MD-11	37	5	—	—
Boeing 747-400F	11	—	—	—
Boeing 747-400BCF 2	—	—	—	—
Boeing 747-8F	9	—	19	—
Other	—	309	—	—
Total	248	316	28	—

## Vehicles

We operate a global ground fleet of approximately 123,000 package cars, vans, tractors and motorcycles. Our ground support fleet consists of 36,000 pieces of equipment designed specifically to support our aircraft fleet, ranging from non-powered container dollies and racks to powered aircraft main deck loaders and cargo tractors. We also have 47,000 containers used to transport cargo in our aircraft.

## Item 3. Legal Proceedings

See note 5 to the audited consolidated financial statements for a discussion of pension related matters and note 9 for a discussion of judicial proceedings and other matters arising from the conduct of our business activities.

## Item 4. Mine Safety Disclosures

Not applicable.

## PART II

## Item 5. Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities

Our class A common stock is not listed on a national securities exchange or traded in an organized over-the-counter market, but each share of our class A common stock is convertible into one share of our class B common stock. Our class B common stock is listed on the New York Stock Exchange under the symbol "UPS".

As of February 8, 2019, there were 155,651 and 19,151 shareowners of record of class A and class B common stock, respectively.

Our practice has been to pay dividends on a quarterly basis. The declaration of dividends is subject to the discretion of the Board of Directors and will depend on various factors, including our net income, financial condition, cash requirements, future prospects and other relevant factors.

On February 15, 2019, our Board declared a dividend of \$0.96 per share, which is payable on March 12, 2019 to shareowners of record on February 26, 2019. This represents a 5.5% increase from the previous \$0.91 per share quarterly dividend paid in December 2018.

A summary of repurchases of our class A and class B common stock during the fourth quarter of 2018 is as follows (in millions, except per share amounts):

	Total Number of Shares Purchased <sup>(1)</sup>	Total Number of Shares Purchased as Part of Publicly Announced Program	Average Price Paid Per Share	Approximate Dollar Value of Shares that May Yet be Purchased Under the Program (as of month-end)
October 1—October 31	0.8	0.8	\$ 116.96	\$ 3,495
November 1—November 30	0.7	0.7	110.33	3,416
December 1—December 31	0.8	0.8	101.13	3,339
Total October 1—December 31	2.3	2.3	\$ 109.41	

(1) Includes shares repurchased through our publicly announced share repurchase program and shares tendered to pay the exercise price and tax withholding on employee stock options.

In May 2016, the Board of Directors approved a share repurchase authorization of \$8.0 billion, which replaced an authorization previously announced in 2013. The share repurchase authorization has no expiration date. As of December 31, 2018, we had \$3.339 billion of this share repurchase authorization remaining.

Share repurchases may take the form of accelerated share repurchases, open market purchases, or other such methods as we deem appropriate. The timing of our share repurchases will depend upon market conditions. We anticipate repurchasing approximately \$1.0 billion of shares in 2019.

Shareowner Return Performance Graph

The following performance graph and related information shall not be deemed “soliciting material” or to be “filed” with the SEC, nor shall such information be incorporated by reference into any future filing under the Securities Act of 1933 or Securities Exchange Act of 1934, each as amended, except to the extent that the Company specifically incorporates such information by reference into such filing.

The following graph shows a five-year comparison of cumulative total shareowners’ returns for our class B common stock, the Standard & Poor’s 500 Index and the Dow Jones Transportation Average. The comparison of the total cumulative return on investment, which is the change in the stock price plus reinvested dividends for each of the quarterly periods, assumes that \$100 was invested on December 31, 2013 in the Standard & Poor’s 500 Index, the Dow Jones Transportation Average and our class B common stock.

	12/31/2013	12/31/2014	12/31/2015	12/31/2016	12/31/2017	12/31/2018
United Parcel Service, Inc.	\$ 100.00	\$ 108.67	\$ 101.61	\$ 124.68	\$ 133.59	\$ 112.91
Standard & Poor’s 500 Index	\$ 100.00	\$ 113.68	\$ 115.24	\$ 129.02	\$ 157.17	\$ 150.27
Dow Jones Transportation Average	\$ 100.00	\$ 125.07	\$ 104.11	\$ 126.87	\$ 151.00	\$ 132.38

For information regarding our equity compensation plans, see Item 12 of this report.



## Item 6. Selected Financial Data

The following table sets forth selected financial data for each of the five years in the period ended December 31, 2018 (in millions, except per share amounts). This financial data should be read together with our consolidated financial statements and related notes, Management's Discussion and Analysis of Financial Condition and Results of Operations, including the Items Affecting Comparability section, and other financial data appearing elsewhere in this report.

	Years Ended December 31,				
	2018	2017	2016	2015	2014
Selected Income Statement Data					
Revenue:					
U.S. Domestic Package	\$43,593	\$40,761	\$38,284	\$36,744	\$35,851
International Package	14,442	13,342	12,346	12,142	13,032
Supply Chain & Freight	13,826	12,482	10,980	10,300	10,295
Total Revenue	71,861	66,585	61,610	59,186	59,178
Operating Expenses:					
Compensation and benefits	37,235	34,577	32,534	31,448	30,247
Other	27,602	24,479	21,388	20,495	22,161
Total Operating Expenses	64,837	59,056	53,922	51,943	52,408
Operating Profit:					
U.S. Domestic Package	3,643	4,303	4,628	4,427	4,244
International Package	2,529	2,429	2,417	2,123	1,884
Supply Chain and Freight	852	797	643	693	642
Total Operating Profit	7,024	7,529	7,688	7,243	6,770
Other Income and (Expense):					
Investment income (expense) and other	(400)	61	(2,186)	435	(1,776)
Interest expense	(605)	(453)	(381)	(341)	(353)
Income Before Income Taxes	6,019	7,137	5,121	7,337	4,641
Income Tax Expense	1,228	2,232	1,699	2,497	1,607
Net Income	\$4,791	\$4,905	\$3,422	\$4,840	\$3,034
Per Share Amounts:					
Basic Earnings Per Share	\$5.53	\$5.63	\$3.88	\$5.37	\$3.31
Diluted Earnings Per Share	\$5.51	\$5.61	\$3.86	\$5.34	\$3.28
Dividends Declared Per Share	\$3.64	\$3.32	\$3.12	\$2.92	\$2.68
Weighted Average Shares Outstanding:					
Basic	866	871	883	901	916
Diluted	870	875	887	906	924
As of December 31,					
	2018	2017	2016	2015	2014
Selected Balance Sheet Data:					
Cash and marketable securities	\$5,035	\$4,069	\$4,567	\$4,726	\$3,283
Total assets	50,016	45,574	40,545	38,497	35,634
Long-term debt	19,931	20,278	12,394	11,316	9,856
Shareowners' equity	3,037	1,024	430	2,501	2,173

This table reflects the impact of the adoption of new accounting standards in 2018. Refer to note 1 to the audited consolidated financial statements.

## Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations

## Overview

During 2018, we produced strong revenue growth across all three segments. We realized improvements in revenue per piece as pricing and growth initiatives drove an increase in yields in all of our major products.

We achieved solid operating profit growth in both our International Package and Supply Chain & Freight segments. Operating profit in our U.S. Domestic segment operation was negatively impacted primarily by planned costs related to our transformation strategy, higher pension expenses, one less operating day and the impact of bringing new facility and technology projects on-line. The benefits of our efficiency and growth initiatives in the U.S. will not be fully realized until future periods.

Consolidated revenue increased 7.9% to \$71.861 billion, up from \$66.585 billion in 2017. Operating profit for 2018 decreased 6.7% to \$7.024 billion, which includes the impact of \$360 million pre-tax transformation strategy costs. Consolidated average daily package volume increased 3.2% in 2018. We reported 2018 net income of \$4.791 billion and diluted earnings per share of \$5.51, compared to 2017 net income of \$4.905 billion and diluted earnings per share of \$5.61. Adjusting for the after-tax impacts of transformation costs of \$273 million and an increase in pension expense due to a mark-to-market loss recognized outside of the 10% corridor of \$1.237 billion (\$1.627 billion before tax), net income was \$6.301 billion.

Our consolidated results are presented in the table below:

	Year Ended December 31,			% Change	
	2018	2017	2016	2018/ 2017	2017/ 2016
Revenue (in millions)	\$71,861	\$66,585	\$61,610	7.9 %	8.1 %
Operating Expenses (in millions)	64,837	59,056	53,922	9.8 %	9.5 %
Operating Profit (in millions)	\$7,024	\$7,529	\$7,688	(6.7)%	(2.1)%
Operating Margin	9.8 %	11.3 %	12.5 %		
Average Daily Package Volume (in thousands)	20,677	20,030	19,083	3.2 %	5.0 %
Average Revenue Per Piece	\$10.98	\$10.53	\$10.29	4.3 %	2.3 %
Net Income (in millions)	\$4,791	\$4,905	\$3,422	(2.3)%	43.3 %
Basic Earnings Per Share	\$5.53	\$5.63	\$3.88	(1.8)%	45.1 %
Diluted Earnings Per Share	\$5.51	\$5.61	\$3.86	(1.8)%	45.3 %

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Items Affecting Comparability

The results and discussions that follow are reflective of how our executive management monitors the performance of our reporting segments. We supplement the reporting of our financial information determined under generally accepted accounting principles ("GAAP") with certain non-GAAP financial measures, including, as applicable, "adjusted" compensation and benefits, operating expenses, operating profit, operating margin, other income (expense), pre-tax income, net income and earnings per share. These adjustments reflect the non-comparable items discussed below. We believe that these adjusted financial measures provide meaningful information to assist investors and analysts in understanding our financial results and assessing our prospects for future performance. We believe these adjusted financial measures are important indicators of our recurring results of operations because they exclude items that may not be indicative of, or are unrelated to, our underlying operating results and provide a useful baseline for analyzing trends in our underlying businesses. Additionally, these adjusted financial measures are used internally by management for the determination of incentive compensation awards, business unit operating performance analysis and business unit resource allocation.

Non-GAAP financial measures should be considered in addition to, and not as an alternative for, our reported results prepared in accordance with GAAP. Our non-GAAP financial information does not represent a comprehensive basis of accounting. Therefore, our non-GAAP financial information may not be comparable to similarly titled measures reported by other companies.

The year-over-year comparisons of our financial results are affected by the following items (in millions):

	Year Ended December 31,		
	2018	2017	2016
Non-GAAP Adjustments			
Operating Expenses:			
Transformation Strategy Costs	\$ 360	\$—	\$—
Total Adjustments to Operating Expenses	360	—	—
Other Income and (Expense):			
Defined Benefit Plans Mark-to-Market Charges	\$ 1,627	\$ 800	\$ 2,651
Total Adjustments to Other Income and (Expense)	1,627	800	2,651
Total Adjustments to Income Before Income Taxes	1,987	800	2,651
Income Tax Benefit from the Mark-to-Market Charges	(390 )	(193 )	(978 )
Income Tax Benefit from Transformation Strategy Costs	(87 )	—	—
Income Tax Benefit from the Tax Cuts and Jobs Act and Other Non-U.S. Tax Law Changes	—	(258 )	—
Total Adjustments to Income Tax Expense	\$(477 )	\$(451 )	\$(978 )
Total Adjustments to Net Income	\$ 1,510	\$ 349	\$ 1,673

These items have been excluded from comparisons of "adjusted" Compensation and benefits, Operating Expenses, Operating Profit, Operating Margin, Other Income and (Expense), Income Tax Expense and effective tax rate in the discussion that follows. The income tax effects of the transformation strategy costs and the mark-to-market charges are calculated by multiplying the statutory tax rates applicable in each tax jurisdiction, including the U.S. federal jurisdiction and various U.S. state and non-U.S. jurisdictions, by the adjustments. The blended average of the applicable statutory tax rates in 2018, 2017 and 2016 were 24.0%, 24.1% and 36.9%, respectively. We believe this adjusted information provides useful comparison of year-to-year ongoing operating performance without considering the short-term impact of transformation strategy costs. We evaluate the performance of our businesses on an adjusted basis.



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Impact of Changes in Foreign Currency Exchange Rates

We supplement the reporting of our revenue, revenue per piece, and operating profit, along with other income and expense, with similar non-GAAP measures that exclude the period-over-period impact of foreign currency exchange rate changes and hedging activities. We believe currency-neutral revenue, revenue per piece and operating profit information allows users of our financial statements to understand growth trends in our products and results. We evaluate the performance of our International Package and Supply Chain & Freight businesses on a currency-neutral basis.

Currency-neutral revenue, revenue per piece and operating profit are calculated by dividing current period reported U.S. dollar revenue, revenue per piece and operating profit by the current period average exchange rates to derive current period local currency revenue, revenue per piece and operating profit. The derived current period local currency revenue, revenue per piece and operating profit are then multiplied by the average foreign exchange rates used to translate the comparable results for each month in the prior year period (including the period over period impact of foreign currency revenue hedging activities). The difference between the current period reported U.S. dollar revenue, revenue per piece and operating profit and the derived current period U.S. dollar revenue, revenue per piece and operating profit is the period over period impact of currency fluctuations.

Transformation Strategy Costs

Transformation strategy costs described in note 16 to the audited consolidated financial statements have been excluded from comparisons of "adjusted" Compensation and benefits, Other Operating Expenses, Operating Profit, Operating Margin, Income Tax Expense and effective tax rate. The pre-tax transformation strategy costs totaled \$360 million (\$273 million after-tax) in 2018, and reflects costs and other benefits of \$262 million included within Compensation and benefits on the statements of consolidated income, and other costs of \$98 million recorded to total other expenses. We believe this adjusted information provides useful comparison of year-to-year ongoing operating performance without considering the short-term impact of transformation strategy costs.

Income Tax Benefit from the Tax Cuts and Jobs Act

We supplement the presentation of our income tax expense and effective tax rate with "adjusted" measures that exclude the impact of the income tax benefit from the Tax Cuts and Jobs Act (the "Tax Act") described in the "Income Tax Expense" section of Management's Discussion and Analysis and note 13 to the audited consolidated financial statements. We believe income tax expense and the effective tax rate excluding the tax benefit is useful in evaluating our ongoing operating performance for the current period to that of other periods presented.

Defined Benefit Plans Mark-to-Market Charges

We recognize changes in the fair value of plan assets and net actuarial gains and losses in excess of a 10% corridor for our pension and postretirement defined benefit plans immediately as part of net periodic benefit cost other than service cost. We supplement the presentation of our Other Income and (Expense) with "adjusted" measures that exclude the impact of the portion of net periodic benefit cost other than service cost represented by the gains and losses recognized in excess of the 10% corridor and the related income tax effects.

This adjusted net periodic benefit cost (\$615 million in 2018, \$843 million in 2017 and \$1.074 billion in 2016) utilizes the expected return on plan assets (7.68% in 2018 and 8.65% in 2017 and 2016). The non-adjusted net periodic benefit cost reflects the actual return on plan assets (-2.38% in 2018, 14.25% in 2017 and 6.06% in 2016) and the discount rate used to measure the projected benefit obligation at the December 31 measurement date (4.45% in 2018, 3.81% in 2017 and 4.34% in 2016). We believe excluding these mark-to-market charges from our adjusted results provides important supplemental information that reflects the anticipated long-term cost of our defined benefit plans and

provides a benchmark for historical defined benefit cost trends that may provide a useful comparison of year-to-year financial performance without considering the short-term impact of changes in market interest rates, equity prices and similar factors.

We recognized pre-tax mark-to-market losses in "Other Income and (Expense)" of \$1.627 billion, \$800 million and \$2.651 billion on our pension and postretirement defined benefit plans related to the remeasurement of plan assets and liabilities recognized outside of a 10% corridor, for 2018, 2017 and 2016, respectively.

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The table below indicates the amounts associated with each component of the pre-tax mark-to-market losses, as well as the weighted-average actuarial assumptions used to determine our net periodic benefit costs, for each year:

Components of mark-to-market gain (loss) (in millions):	Year Ended December 31,		
	2018	2017	2016
Discount rates	\$845	\$(2,288)	\$(1,953)
Return on assets	(1,057 )	1,525	(732 )
Demographic and assumption changes	(22 )	(37 )	34
Coordinating benefits attributable to the Central States Pension Fund	(1,393 )	—	—
Total mark-to-market gain (loss)	\$(1,627)	\$(800 )	\$(2,651)

Weighted-average actuarial assumptions used to determine net periodic benefit cost:	Year Ended December 31,			
	2018	2017	2016	
Expected rate of return on plan assets	7.68	% 8.65	% 8.65	%
Actual rate of return on plan assets	(2.38 )	% 14.25	% 6.06	%
Discount rate used for net periodic benefit cost	3.81	% 4.34	% 4.81	%
Discount rate at measurement date	4.45	% 3.81	% 4.34	%

The \$1.627 billion, \$800 million and \$2.651 billion pre-tax mark-to-market losses for the years ended December 31, 2018, 2017 and 2016, respectively, were comprised of the following components:

2018 - \$1.627 billion pre-tax mark-to-market loss:

• **Return on Assets** (\$1.057 billion pre-tax loss): In 2018, the actual (2.38)% rate of return on plan assets was lower than our expected rate of return of 7.68%, primarily due to weak global equity markets.

• **Coordinating benefits attributable to the Central States Pension Fund** (\$1.393 billion pre-tax loss): This represents our current best estimate of potential coordinating benefits that may be required to be paid related to the Central States Pension Fund.

• **Discount Rates** (\$845 million pre-tax gain): The weighted-average discount rate for our pension and postretirement medical plans increased from 3.81% at December 31, 2017 to 4.45% at December 31, 2018, primarily due to both an increase in U.S. treasury yields and an increase in credit spreads on AA-rated corporate bonds in 2018.

• **Demographic and Assumption Changes** (\$22 million pre-tax loss): This represents the difference between actual and estimated participant data and demographic factors, including items such as healthcare cost trends, compensation rate increases and rates of termination, retirement and mortality.

2017 - \$800 million pre-tax mark-to-market loss:

• **Discount Rates** (\$2.288 billion pre-tax loss): The weighted-average discount rate for our pension and postretirement medical plans decreased from 4.34% at December 31, 2016 to 3.81% at December 31, 2017, primarily due to both a decline in U.S. treasury yields and a decrease in credit spreads on AA-rated corporate bonds in 2017.

• **Return on Assets** (\$1.525 billion pre-tax gain): In 2017, the actual 14.25% rate of return on plan assets exceeded our expected rate of return of 8.65%, primarily due to strong global equity and U.S. bond markets.

• **Demographic and Assumption Changes** (\$37 million pre-tax loss): This represents the difference between actual and estimated participant data and demographic factors, including items such as healthcare cost trends, compensation rate increases and rates of termination, retirement and mortality.



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2016 - \$2.651 billion pre-tax mark-to-market loss:

**Discount Rates** (\$1.953 billion pre-tax loss): The weighted-average discount rate for our pension and postretirement medical plans decreased from 4.81% at December 31, 2015 to 4.34% at December 31 2016, primarily due to a decrease in credit spreads on AA-rated corporate bonds in 2016.

**Return on Assets** (\$732 million pre-tax loss): In 2016, the actual 6.06% rate of return on plan assets fell short of our expected rate of return of 8.65%, primarily due to weak bond markets.

**Demographic and Assumption Changes** (\$34 million pre-tax gain): This represents the difference between actual and estimated participant data and demographic factors, including items such as healthcare cost trends, compensation rate increases and rates of termination, retirement and mortality.

#### Expense Allocations

Certain operating expenses are allocated between our reporting segments using activity-based costing methods. These activity-based costing methods require us to make estimates that impact the amount of each expense category that is attributed to each segment. Changes in these estimates will directly impact the amount of expense allocated to each segment, and therefore the operating profit of each reporting segment. Our allocation methodologies are refined periodically, as necessary, to reflect changes in our businesses. There were no significant changes in our expense allocation methodologies during 2018, 2017 or 2016.

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## U.S. Domestic Package Operations

	Year Ended December 31,			% Change	
	2018	2017	2016	2018/ 2017	2017/ 2016
Average Daily Package Volume (in thousands):					
Next Day Air	1,542	1,460	1,379	5.6 %	5.9 %
Deferred	1,432	1,400	1,350	2.3 %	3.7 %
Ground	14,498	14,060	13,508	3.1 %	4.1 %
Total Avg. Daily Package Volume	17,472	16,920	16,237	3.3 %	4.2 %
Average Revenue Per Piece:					
Next Day Air	\$19.53	\$19.11	\$19.20	2.2 %	(0.5)%
Deferred	13.12	12.44	11.85	5.5 %	5.0 %
Ground	8.51	8.19	7.97	3.9 %	2.8 %
Total Avg. Revenue Per Piece	\$9.86	\$9.48	\$9.25	4.0 %	2.5 %
Operating Days in Period	253	254	255		
Revenue (in millions):					
Next Day Air	\$7,618	\$7,088	\$6,752	7.5 %	5.0 %
Deferred	4,752	4,422	4,080	7.5 %	8.4 %
Ground	31,223	29,251	27,452	6.7 %	6.6 %
Total Revenue	\$43,593	\$40,761	\$38,284	6.9 %	6.5 %
Operating Expenses (in millions):					
Operating Expenses	\$39,950	\$36,458	\$33,656	9.6 %	8.3 %
Transformation Strategy Costs	(235 )	—	—		
Adjusted Operating Expenses	\$39,715	\$36,458	\$33,656	8.9 %	8.3 %
Operating Profit (in millions) and Operating Margin:					
Operating Profit	\$3,643	\$4,303	\$4,628	(15.3)%	(7.0)%
Adjusted Operating Profit	\$3,878	\$4,303	\$4,628	(9.9 )%	(7.0)%
Operating Margin	8.4	% 10.6	% 12.1	%	
Adjusted Operating Margin	8.9	% 10.6	% 12.1	%	
Revenue					

The change in overall revenue was impacted by the following factors for the years ended December 31, 2018 and 2017, compared with the corresponding prior year periods:

	Volume	Rates / Product Mix	Fuel Surcharge	Total Revenue Change
Revenue Change Drivers:				
2018/ 2017	2.9 %	2.5 %	1.5 %	6.9 %
2017/ 2016	3.8 %	1.8 %	0.9 %	6.5 %

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Volume

2018 compared to 2017

Our overall volume increased across all products in 2018 despite one less operating day, largely due to continued growth in overall retail sales, of which e-commerce continues to represent a larger percentage of the total growth. Growth was focused within the retail, healthcare and manufacturing industries.

Business-to-consumer shipments, which represented more than 50% of total U.S. Domestic Package volume, grew 6.2% for the year and drove overall increases in both air and ground shipments. While business-to-business shipments were relatively flat in 2018 compared to 2017, volume grew 3% in the fourth quarter of 2018 compared to 2017.

Among our air products, volume increased in 2018 for our Next Day Air and Deferred services. Solid air volume growth continued for those products most aligned with business-to-consumer shipping, including our residential Next Day Air, Next Day Air Saver and Second Day package products, as consumers continue to demand faster and more economical delivery options. This growth was slightly offset by declines in residential Next Day Air letter, Next Day Air Saver letter and Second Day letter volume.

The increase in ground volume in 2018 was driven by growth in residential ground and SurePost volume, which benefited from continued e-commerce demand. Business-to-business ground shipments were relatively flat in 2018 compared to 2017, however they grew approximately 3% in the fourth quarter of 2018 compared to 2017.

2017 compared to 2016

Our overall volume increased across all products in 2017, largely due to continued growth in overall retail sales, of which e-commerce continues to represent a larger percentage of the total growth. Business-to-consumer shipments, which represented just over 50% of total U.S. Domestic Package volume, grew 9.4% for the year, which drove increases in both air and ground shipments. Business-to-business shipments decreased slightly in 2017 compared to 2016 largely due to declines in volume in professional services as a result of increased digitization, and high tech industries.

Among our air products, volume increased in 2017 for our Next Day Air and Deferred services. Solid air volume growth continued for those products most aligned with business-to-consumer shipping, including our residential Next Day Air, Next Day Air Saver and Three Day Select package products, as consumers continue to demand faster options. This growth was slightly offset by a decline in Next Day Air letter volume, largely due to declines in the professional services industry as a result of continued growth in digitization.

The increase in ground volume in 2017 was driven by growth in residential ground and SurePost volume, which benefited from continued e-commerce demand. Business-to-business shipments decreased slightly due to adverse weather conditions in third quarter 2017, however this decrease was partially offset by an increase in our return shipping services.

Rates and Product Mix

2018 compared to 2017

Overall revenue per piece increased 4.0% in 2018, and was impacted by changes in base rates, the implementation of new surcharges for oversized packages and other fees, customer and product mix and fuel surcharge rates.

Revenue per piece for ground and air products was positively impacted by a base rate increase on December 24, 2017. UPS Ground rates and UPS Air services rates increased an average net 4.9%. Effective June 4, 2018, we increased the surcharge for Over Maximum Limits, Oversize Pallet Handling, and added a shipping correction audit fee. Effective July 8, 2018, we implemented a U.S. Residential Large Package surcharge and an additional handling surcharge for packages exceeding 70 pounds. Additionally peak surcharges were in effect from October 1, 2018 through December 22, 2018 for U.S. Residential, Large Packages and packages Over Maximum Limits. The charge was designed to enable UPS to continue to offset some of the additional expenses incurred during significant volume surges.

Additionally on December 5, 2018, we announced an average 4.9% base rate increase effective December 26, 2018 for UPS Ground and UPS Air services.

In the first quarter of 2017, we began our expanded Saturday ground operations to several metropolitan areas in the United States. As of December 31, 2018, Saturday service is available in approximately 6,100 cities and towns in the U.S. covering approximately 60% of the population.

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Revenue per piece for all products was positively impacted by higher fuel surcharge rates in 2018 due to escalating fuel prices and increases in rates.

Revenue per piece for our Next Day Air services increased in 2018 compared with 2017. The increase in Next Day Air revenue per piece was primarily due to an increase in base rates driven by pricing initiatives and an increase in average billable weight per piece which more than offset an unfavorable shift in product mix.

Revenue per piece for our Deferred air services increased in 2018 compared with 2017 due to an increase in base rate pricing driven by pricing initiatives and average billable weight per piece offset slightly by an unfavorable shift in product mix.

Ground revenue per piece increased in 2018 compared with 2017, primarily due to base rate increases driven by our pricing initiatives. These factors were partially offset by changes in product mix, as we experienced faster volume growth in our SurePost product.

2017 compared to 2016

Overall revenue per piece increased 2.5% in 2017, and was impacted by changes in base rates, customer and product mix and fuel surcharge rates.

Revenue per piece for ground and air products was positively impacted by a base rate increase on December 26, 2016. UPS Ground rates and UPS Air services rates increased an average net 4.9%. Effective January 8, 2017, we changed the dimensional weight calculation for packages subject to UPS daily rates. On June 19, 2017, we announced a new peak charge applicable during selected weeks in November and December 2017 for U.S. Residential, Large Packages and packages Over Maximum Limits. The new charge is designed to enable UPS to continue to offset some of the additional expenses incurred during significant volume surges. Additionally on October 25, 2017, we announced an average 4.9% base rate increase effective December 24, 2017 for UPS Ground and UPS Air services.

In the first quarter of 2017, we began our expanded Saturday ground operations to several metropolitan areas in the United States. As of December 2017, Saturday service was available in approximately 4,700 cities and towns in the U.S. covering approximately 50% of the population. A Saturday pickup stop charge went into effect on May 1, 2017 and varies depending on the pickup service selected.

Revenue per piece for all products was positively impacted by higher fuel surcharge rates for 2017.

Revenue per piece for our Next Day Air services decreased in 2017 compared with 2016. The decrease in Next Day Air revenue per piece was primarily driven by a shift in product mix, as our lower yielding products experienced much larger volume growth than our higher yielding products. This shift was offset slightly by an increase in the average billable weight per piece.

Revenue per piece of our Deferred air services increased in 2017 compared with 2016. Deferred revenue per piece increased primarily due to an increase in average billable weight per piece, but was partially offset by an unfavorable shift in product mix.

Ground revenue per piece increased in 2017, primarily due to base rate increases, higher fuel surcharge rates and an increase in average billable weight per piece. These factors were partially offset by changes in product mix, as we experienced faster volume growth in our SurePost product.

Fuel Surcharges

UPS applies a fuel surcharge on our domestic air and ground services. The air fuel surcharge is based on the U.S. Department of Energy's ("DOE") Gulf Coast spot price for a gallon of kerosene-type jet fuel, while the ground fuel surcharge is based on the DOE's On-Highway Diesel Fuel Price. Based on published rates, the average fuel surcharge rates for domestic air and ground products were as follows:

Year Ended December 31, % Point Change				
2018	2017	2016	2018/ 2017	2017/ 2016

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Next Day Air / Deferred	7.7 %	5.1 %	3.6 %	2.6 %	1.5 %
Ground	7.0 %	5.6 %	4.9 %	1.4 %	0.7 %

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Effective February 6, 2017, the U.S. fuel surcharge rates are reset weekly instead of monthly. In addition, the price indices have moved from a two month to a two week lag in order to more closely align fuel surcharge revenues with fuel expenses. In June and October 2018, ground fuel surcharge rates were raised by 0.50% and 0.25%, respectively, for all thresholds. In October 2018, Domestic air fuel surcharge rates were increased by 0.25% for all thresholds. While fluctuations in fuel surcharge percentages can be significant from period to period, fuel surcharges represent one of the many individual components of our pricing structure that impact our overall revenue and yield. Additional components include the mix of services sold, the base price and extra service charges we obtain for these services and the level of pricing discounts offered.

Total domestic fuel surcharge revenue increased by \$632 million in 2018 as a result of higher fuel surcharge rates caused by an increase in jet and diesel fuel prices, as well as an overall increase in package volume which drove increased delivery miles driven and aircraft block hours.

Operating Expenses

2018 compared to 2017

Operating expenses for the segment increased \$3.492 billion in 2018 compared with 2017, which included \$235 million of transformation strategy costs. Excluding the impact of transformation strategy costs, operating expenses for the segment increased \$3.257 billion in 2018, primarily due to pickup and delivery costs (up \$1.305 billion), the costs of operating our domestic integrated air and ground network (up \$1.649 billion) and the costs of package sorting (up \$639 million), offset by a reduction in indirect operating costs (down \$336 million) for the year. These expenses were primarily due to higher volume, increased employee compensation costs, higher pension expense, higher fuel prices, a 6.2% increase in average daily block hours and expansion of our technology-enabled network.

The growth in pickup and delivery and network costs was impacted by several factors:

We incurred higher employee compensation and benefit costs largely resulting from volume growth, which impacted an increase in average daily union labor hours (up 5.2%), scheduled union pay rate and benefit increases and growth in the overall size of the workforce due to facility expansions. Labor hour increases were also related to the continued expansion in Saturday operations. In addition, pension expense increased due to lower year-end discount rates used to measure the pension benefit obligation, driving higher service costs.

We incurred higher fuel expense in 2018 primarily due to higher fuel prices and increased volume which resulted in higher fuel usage (increase in aircraft block hours of 6.2% and package delivery miles driven of 4.4%), partially offset by alternative fuel tax credits. The manner in which we purchase fuel also influences the net impact of fuel on our results. The majority of our contracts for fuel purchases utilize index-based pricing formulas plus or minus a fixed locational/supplier differential. While many of the indices are aligned, each index may fluctuate at a different pace, driving variability in the prices paid for fuel. Because of this, our operating results may be affected should the market price of fuel suddenly change by a significant amount or change by amounts that do not result in an adjustment in our fuel surcharges, which can significantly affect our earnings either positively or negatively in the short-term.

We incurred higher costs associated with outside contract carriers, primarily due to volume growth (including SurePost), higher fuel surcharges passed to us by carriers and general rate increases.

In order to contain costs, we continually adjust our air and ground networks to better match higher volume levels. In addition, we continue to deploy and utilize technology to increase package sorting and delivery productivity.

Total cost per piece increased 6.6% in 2018 compared with 2017, which includes transformation strategy costs of \$235 million. The cost per piece increase was primarily impacted by the cost increases described previously. The increased expenses in 2018 were also driven by costs related to the improvement of our smart global logistics network, including additional aircraft leases to improve our air service reliability; costs related to the implementation of Saturday operations in additional markets, depreciation costs due to new facilities placed in service and higher pension expense. Costs were also negatively impacted by rising fuel prices offset by net changes in depreciation, primarily driven by changes in the useful lives of vehicles, plant equipment and building improvements.





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2017 compared to 2016

Operating expenses for the period increased \$2.802 billion in 2017, primarily due to pickup and delivery costs (up \$1.312 billion), the cost of operating our domestic integrated air and ground network (up \$810 million), the costs of package sorting (up \$746 million), offset by a reduction in indirect operating costs (down \$66 million). These increases were driven primarily by overall volume growth in 2017. Adjusted operating expenses were impacted by several factors:

• We incurred higher employee compensation, largely resulting from volume growth, an increase in average daily union labor hours (up 6.5%), growth in the overall size of the workforce and an increase in wage rates.

• Employee benefit costs increased, largely due to increased employee healthcare, partially offset by a decrease in pension expense and workers' compensation expense.

• We incurred higher fuel expense in 2017 primarily due to higher fuel prices and increased volume, which resulted in higher fuel usage (increase in aircraft block hours of 7.0% and package delivery miles driven of 4.1%).

• We incurred higher costs associated with outside contract carriers, primarily due to volume growth (including SurePost), higher fuel surcharges passed to us by carriers and general rate increases.

Total cost per piece increased 4.3% in 2017 compared to 2016 and was primarily impacted by the cost increases described previously. The increased expenses in 2017 were also driven by capacity constraints due to volume surges in the fourth quarter of 2017, start-up costs of several investments underway to further expand and modernize our air and ground networks, and the costs of implementing Saturday operations. Costs were further impacted by rising fuel prices.

#### Operating Profit and Margin

2018 compared to 2017

Operating profit was negatively impacted primarily by planned costs related to our transformation strategy, higher pension expenses, one less operating day and the impact of bringing new facility and technology projects on-line. Operating profit decreased \$660 million in 2018 compared with 2017 with operating margins decreasing 220 basis points to 8.4%. Excluding the impact of transformation strategy costs, operating profit decreased \$425 million in 2018 compared to 2017 with operating margins decreasing 170 basis points. While benefits from fuel (fuel surcharge revenue increased at a faster pace than expense) and lower net depreciation expense had a positive impact on operating profit, higher purchased transportation costs due to volume growth, one less operating day and an increase in pension costs driven by lower discount rates weighed on profits. Additionally, operating profit was negatively impacted by costs related to continued investments in our smart global logistics network, including implementation of Saturday operations in additional markets. The benefits of these projects will not be fully realized until future periods.

2017 compared to 2016

Operating profit decreased \$325 million in 2017 compared with 2016. Operating margin decreased 150 basis points to 10.6%. Operating profit was negatively impacted by an increase in continued investments in new buildings and new strategic investments, including deployment of Saturday operations. There was an adverse impact from higher purchased transportation costs due to volume surges in the fourth quarter of 2017 and from fuel as expense increased at a faster pace than fuel surcharge revenue.

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## International Package Operations

	Year Ended December 31,			% Change		
	2018	2017	2016	2018/ 2017	2017/ 2016	
Average Daily Package Volume (in thousands):						
Domestic	1,723	1,715	1,635	0.5 %	4.9 %	%
Export	1,482	1,395	1,211	6.2 %	15.2 %	%
Total Avg. Daily Package Volume	3,205	3,110	2,846	3.1 %	9.3 %	%
Average Revenue Per Piece:						
Domestic	\$6.59	\$6.07	\$5.85	8.6 %	3.8 %	%
Export	29.27	28.70	30.34	2.0 %	(5.4 )%	
Total Avg. Revenue Per Piece	\$17.08	\$16.22	\$16.27	5.3 %	(0.3 )%	
Operating Days in Period	253	254	255			
Revenue (in millions):						
Domestic	\$2,874	\$2,646	\$2,441	8.6 %	8.4 %	%
Export	10,973	10,170	9,369	7.9 %	8.5 %	%
Cargo & Other	595	526	536	13.1 %	(1.9 )%	
Total Revenue	\$14,442	\$13,342	\$12,346	8.2 %	8.1 %	%
Operating Expenses (in millions):						
Operating Expenses	\$11,913	\$10,913	\$9,929	9.2 %	9.9 %	%
Transformation Strategy Costs	(76 )	—	—			
Adjusted Operating Expenses	\$11,837	\$10,913	\$9,929	8.5 %	9.9 %	%
Operating Profit (in millions) and Operating Margin:						
Operating Profit	\$2,529	\$2,429	\$2,417	4.1 %	0.5 %	%
Adjusted Operating Profit	\$2,605	\$2,429	\$2,417	7.2 %	0.5 %	%
Operating Margin	17.5 %	18.2 %	19.6 %			
Adjusted Operating Margin	18.0 %	18.2 %	19.6 %			
Currency Translation Benefit / (Cost)—(in millions)*:						
Revenue					\$147	\$(325)
Operating Expenses					(157 )	(50 )
Operating Profit					\$(10 )	\$(375)

\*Net of currency hedging; amount represents the change compared to the prior year.

## Revenue

The change in overall revenue was impacted by the following factors for the years ended December 31, 2018 and 2017, compared with the corresponding prior year periods:

	Volume	Rates / Product Mix	Fuel Surcharge	Currency	Total Revenue Change
Revenue Change Drivers:					
2018/ 2017	2.6 %	1.8 %	2.7 %	1.1 %	8.2 %
2017/ 2016	8.8 %	(0.7 )%	2.6 %	(2.6 )%	8.1 %

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Volume

2018 compared to 2017

Our overall average daily volume increased in 2018 largely due to strong demand from several sectors including retail, industrial manufacturing, high-tech and healthcare. Business-to-consumer shipments remained relatively flat for the year.

We continued to experience export volume growth in 2018. The growth was mainly driven by our European, U.S. and Asian operations, which experienced increases in volume on almost all major trade lanes. European export volume showed growth in the Europe-to-U.S. and intra-Europe trade lanes. Export volume into the U.S. grew in most major trade lanes, led by Europe and the Americas. Asia export volume growth was the most significant in the Asia-to-Americas and intra-Asia trade lanes. Export volume growth was strong across most major products, with a continued shift towards our premium express products, such as Worldwide Express and Transborder Express services. Domestic volume increased slightly, primarily due to growth in Mexico, Canada and Netherlands, while domestic products in the Euro zone declined slightly.

2017 compared to 2016

Our overall average daily volume increased in 2017, largely due to continued strength in business-to-consumer volume, as well as strong demand from several sectors including retail, industrial manufacturing, high-tech and healthcare.

We continued to experience export volume growth in 2017. The growth was mainly driven by our European, Asian and U.S. operations, which experienced increases in volume to major trade lanes of the world. European export volume increased in 2017, with growth in all trade lanes. Asia export volume also increased in 2017, with particular strength in Asia-to-U.S., Asia-to-Americas and intra-Asia trade lanes. Export volume into the U.S. grew in all trade lanes, led by Europe and the Americas. Export volume growth was strong across all major products, with a continued shift towards our premium express products, such as Worldwide Express and Transborder Express services.

The increase in domestic volume in 2017 was primarily due to growth in Turkey, Germany, France, Italy and U.K.

Rates and Product Mix

2018 compared to 2017

Total average revenue per piece increased 5.3% in 2018, impacted by a 110 basis point increase from currency. Additionally, total revenue per piece was impacted by an increase in fuel surcharge revenue, as well as a shift in product mix, as the growth in higher yielding premium products continued to exceed overall growth.

On December 24, 2017, we implemented an average 4.9% net increase in base and accessorial rates for international shipments originating in the United States. Rate changes for shipments originating outside the U.S. are made throughout the year and vary by geographic market. On October 15, 2018, we implemented a 0.50% increase in International Air-Import fuel surcharge. Additionally, on December 5, 2018, we announced an average 4.9% net increase in base and accessorial rates for international shipping originating in the United States, which became effective on December 26, 2018.

Export revenue per piece increased 2.0% in 2018, impacted by a 60 basis point increase from currency, shift in product mix and higher fuel surcharge revenue.

Domestic revenue per piece increased 8.6% in 2018, impacted by a 320 basis point increase from currency and higher fuel surcharges.

2017 compared to 2016

Total average revenue per piece decreased 0.3% in 2017, impacted by a 250 basis point reduction from currency and a shift in product mix. These factors were partially offset by an increase in fuel surcharge rates as well as an increase in base rates.



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On December 26, 2016, we implemented an average 4.9% net increase in base and accessorial rates for international shipments originating in the United States. Rate changes for shipments originating outside the U.S. are made throughout the year and vary by geographic markets. Effective September 17, 2017, a peak surcharge was applied to any shipment originating from China or Hong Kong to the United States for certain service levels during the peak period. The surcharge was applied as a rate per pound based upon the billable weight of the shipment. Additionally, on October 25, 2017, we announced an average 4.9% net increase in base and accessorial rates for international shipping originating in the United States; changes became effective on December 24, 2017.

Export revenue per piece decreased 5.4% in 2017, impacted by a 320 basis point reduction from currency and product mix. This was partially offset by an increase in fuel surcharges, an increase in base rates and strong volume growth in premium products.

Domestic revenue per piece increased 3.8% in 2017, impacted by a 50 basis point increase from currency, increases in base rates and higher fuel surcharges.

#### Fuel Surcharges

We maintain fuel surcharges on our international air and ground services. The fuel surcharges for international air products originating inside or outside the United States are largely indexed to the DOE's Gulf Coast spot price for a gallon of kerosene-type jet fuel, while the fuel surcharges for ground products originating outside the United States are indexed to fuel prices in the international region or country where the shipment takes place.

While fluctuations in fuel surcharge percentages can be significant from period to period, fuel surcharges represent one of the many individual components of our pricing structure that impact our overall revenue and yield. Additional components include the mix of services sold, the base price and extra service charges we obtain for these services and the level of pricing discounts offered.

Total international fuel surcharge revenue increased by \$382 million in 2018, primarily due to volume increases and higher fuel prices. Total international fuel surcharge revenue increased by \$325 million in 2017, primarily due to volume increase, higher fuel prices and pricing changes made to base freight rates and to the fuel surcharge indices from a two month lag to a two week lag.

#### Operating Expenses

##### 2018 compared to 2017

Overall operating expenses increased by \$1.0 billion, which included a \$76 million increase from transformation strategy costs. Excluding the impact of the transformation strategy costs, adjusted operating expenses for the segment increased \$924 million in 2018 primarily due to increased volumes, currency fluctuations and higher fuel costs driven by increased usage and higher prices.

In addition to variability in usage and fuel prices, the manner in which we purchase fuel also influences the net impact of fuel on our results. The majority of our contracts for fuel purchases utilize index-based pricing formulas plus or minus a fixed locational/supplier differential. While many of the indices are aligned, each index may fluctuate at a different pace, driving variability in the prices paid for fuel. Because of this, our operating results may be affected should the market price of fuel suddenly change by a significant amount or change by amounts that do not result in an adjustment in our fuel surcharges, which can affect our earnings either positively or negatively in the short-term.

Operating expenses were impacted by changes in the cost of operating our international integrated air and ground network, which increased \$546 million, as well as pickup and delivery costs, which increased \$287 million. The increase in network costs was largely driven by volume growth in the majority of our products and higher fuel costs due to increased prices and usage. Additionally, the increase in pickup and delivery costs is due to increased volume. Operating expenses were also impacted by a \$91 million increase in indirect overhead and package sorting costs and other costs.

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2017 compared to 2016

Overall operating expenses increased by \$984 million, primarily due to increased volumes, higher fuel usage and currency fluctuations.

Operating expenses were impacted by changes in the cost of operating our international integrated air and ground network, which increased \$424 million, as well as pickup and delivery costs, which increased \$287 million. The increase in network costs was largely driven by volume growth in our Express products, which drove a 3.0% increase in aircraft block hours and higher fuel usage. Additionally, the increase in pickup and delivery costs is due to increased volume. Operating expenses were also impacted in 2017 by a \$273 million increase in indirect overhead and package sorting costs and other costs.

Operating Profit and Margin

2018 compared to 2017

Operating profit increased \$100 million (4.1%) in 2018 compared with 2017, including \$76 million in transformation strategy costs. Operating margin decreased 70 basis points to 17.5%. Adjusted operating profit without transformation strategy costs increased by \$176 million (7.2%) in 2018, while the adjusted operating margin decreased 20 basis points to 18.0%. Included in adjusted operating profit is a \$10 million decrease due to currency. Currency adjusted margin was 18.3% up from 18.2% in the prior year.

2017 compared to 2016

Operating profit increased \$12 million in 2017 compared with 2016. Operating margin increased 140 basis points to 18.2%. Operating margin was affected by negative currency exchange movements due to volatility of both hedged and unhedged currencies. Included in adjusted operating profit is a \$375 million decrease due to currency.

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## Supply Chain &amp; Freight Operations

	Year Ended December 31,			% Change	
	2018	2017	2016	2018/ 2017	2017/ 2016
Freight LTL Statistics:					
Revenue (in millions)	\$2,706	\$2,598	\$2,385	4.2 %	8.9 %
Revenue Per Hundredweight	\$25.52	\$24.08	\$23.44	6.0 %	2.7 %
Shipments (in thousands)	9,720	10,210	9,961	(4.8)%	2.5 %
Shipments Per Day (in thousands)	38.4	40.5	39.4	(5.2)%	2.8 %
Gross Weight Hauled (in millions of lbs)	10,605	10,788	10,174	(1.7)%	6.0 %
Weight Per Shipment (in lbs)	1,091	1,057	1,021	3.2 %	3.5 %
Operating Days in Period	253	252	253		
Revenue (in millions):					
Forwarding	6,580	5,674	4,873	16.0 %	16.4%
Logistics	3,234	3,017	2,644	7.2 %	14.1%
Freight	3,218	3,000	2,737	7.3 %	9.6 %
Other	794	791	726	0.4 %	9.0 %
Total Revenue	\$13,826	\$12,482	\$10,980	10.8 %	13.7%
Operating Expenses (in millions):					
Operating Expenses	\$12,974	\$11,685	\$10,337	11.0 %	13.0%
Transformation Strategy Costs	(49 )	—	—		
Adjusted Operating Expenses	\$12,925	\$11,685	\$10,337	10.6 %	13.0%
Operating Profit (in millions) and Operating Margins:					
Operating Profit	\$852	\$797	\$643	6.9 %	24.0%
Adjusted Operating Profit	\$901	\$797	\$643	13.0 %	24.0%
Operating Margin	6.2	% 6.4	% 5.9	%	
Adjusted Operating Margin	6.5	% 6.4	% 5.9	%	
Currency Translation Benefit / (Cost)—(in millions)*:					
Revenue				\$39	\$10
Operating Expenses				(44 )	(12 )
Operating Profit				\$(5 )	\$(2 )

\* Amount represents the change compared to the prior year.

In December 2016, we acquired Marken, a global provider of supply chain solutions to the life sciences industry and leader in clinical trials, material storage and distribution. Marken's financial results are included in the above table within the Logistics unit from the date of the acquisition and have impacted the year-over-year comparability of revenue, operating expenses and operating profit for the years ended December 31, 2017 and 2016.

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Revenue

2018 compared to 2017

Total revenue for the Supply Chain & Freight segment increased \$1.344 billion in 2018 compared to 2017. Forwarding revenue increased \$906 million in 2018 compared with 2017, primarily due to increased truckload brokerage volume as well as tonnage increases in our international air freight and ocean freight forwarding businesses. Sell price improvements in our international air freight forwarding business also contributed to the increase in revenue. Revenue in our truckload brokerage business was driven by robust demand and tight capacity. Logistics revenue increased by \$217 million in 2018 compared with 2017, as we experienced growth in the healthcare, aerospace, retail and manufacturing sectors.

UPS Freight revenue increased \$218 million in 2018 compared with 2017, despite fourth-quarter volume declines as a result of the contract ratification process wherein we took actions to clear our LTL network. Revenue was driven by increases in average weight per shipment from improved customer mix due to middle market growth. LTL revenue per hundredweight increased 6.0% as LTL base rate increases for certain shipments in the U.S., Canada and Mexico, averaging 5.9%, took effect March 26, 2018. Fuel surcharge revenue also increased \$75 million due to changes in diesel fuel prices.

2017 compared to 2016

Total revenue for the Supply Chain & Freight segment increased \$1.502 billion in 2017 compared to 2016. Forwarding revenue increased \$801 million in 2017 compared with 2016, primarily due to increased truckload brokerage volume movement and tonnage increases in our international air freight and North American air freight forwarding businesses. The volume and tonnage increases were driven by improving overall market demand. Logistics revenue increased \$373 million in 2017 due to growth in mail services, healthcare, retail and aerospace solutions, offset by declines among our high tech customers. Additionally, the Marken acquisition on December 21, 2016 contributed to the increase in revenue. Revenue was positively impacted by currency exchange rate movements. UPS Freight revenue increased \$263 million in 2017 compared to 2016, driven by increases in shipments and weight per shipment. These increases were impacted by an overall improvement in market demand and customer mix. LTL revenue per hundredweight increased slightly as LTL base rate increases, averaging 4.9%, took effect September 19, 2016. Additionally, effective June 26, 2017, LTL base rates increased by an additional 4.9% for certain shipments in the U.S., Canada and Mexico. Fuel surcharge revenue also increased \$70 million due to changes in overall LTL shipment volume and diesel fuel prices.

Revenue for the other businesses within Supply Chain & Freight increased \$65 million in 2017 due to revenue growth at UPS Capital and UPS Customer Solutions, as well as service contracts with the U.S. Postal Service.

Operating Expenses

2018 compared to 2017

Total operating expenses for the Supply Chain & Freight segment increased \$1.289 billion in 2018 compared to 2017, which includes \$49 million of costs related to our transformation strategy.

Forwarding operating expenses increased \$845 million in 2018 compared with 2017, largely due to increased purchased transportation expenses, transformation strategy costs, and a \$20 million favorable legal settlement in 2017. Excluding \$16 million in costs related to our transformation strategy, Forwarding operating expenses increased \$829 million. Purchased transportation expense increased \$720 million compared to 2017 primarily due to increased truckload brokerage volume and higher tonnage in our international air freight forwarding business as well as the resulting costs passed to us from outside contract carriers.

Logistics operating expenses increased \$205 million in 2018 compared with 2017. Excluding \$22 million in costs related to our transformation strategy, Logistics operating expenses increased \$183 million. The increases were driven by costs associated with retail facility expansions, increased rates for mail services and strategic information technology investments.





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UPS Freight operating expenses increased \$258 million in 2018 compared with 2017. Excluding \$6 million in costs related to our transformation strategy, UPS Freight operating expenses increased \$252 million. Total cost per LTL shipment increased 11.4% in 2018 compared to 2017. The operating expenses increased largely due to costs associated with operating our linehaul network (\$85 million) and increases in pickup and delivery costs (\$60 million). The linehaul network and pickup and delivery costs were driven by higher fuel prices and expense for outside transportation carriers, including fuel surcharges passed on to us by these outside carriers.

2017 compared to 2016

Total operating expenses for the Supply Chain & Freight segment increased \$1.348 billion in 2017 compared to 2016. Forwarding operating expenses increased \$752 million, largely due to increased purchased transportation expenses. This was offset by operating efficiencies and the receipt of a \$20 million favorable legal settlement in the second quarter of 2017. Purchased transportation expense increased by \$770 million compared to 2016 due to increased truckload brokerage movements and the resulting increased fuel surcharges passed to us from outside transportation providers. Increased tonnage and third-party air carrier procurement rates in our North American and international air freight forwarding businesses, also contributed to increased purchased transportation expenses.

Logistics operating expenses increased \$308 million in 2017, primarily due to the acquisition of Marken in 2016 and increased purchased transportation costs driven by increased volume and rates for mail services.

UPS Freight operating expenses increased \$256 million in 2017 compared with 2016. The increase in operating expense was largely due to costs associated with operating our linehaul network (\$126 million) and increases in pickup and delivery costs (\$99 million). The network costs and pickup and delivery expenses were driven by higher fuel cost and higher expense for outside transportation carriers, largely due to LTL volume growth and fuel surcharges passed to us by outside carriers. Total cost per LTL shipment increased 5.7% in 2017 compared to 2016. Operating expenses related to our casualty self-insurance reserves also increased in 2017 compared with 2016.

Other expenses for the other businesses within Supply Chain & Freight increased \$32 million in 2017 compared with 2016 primarily due to UPS Capital, UPS Customer Solutions and service contracts with the U.S. Postal Service, slightly offset by decreases in The UPS Store.

Operating Profit and Margin

2018 compared to 2017

Total operating profit for the Supply Chain & Freight segment increased \$55 million in 2018 compared to 2017, which includes a \$49 million impact related to transformation strategy costs. Excluding transformation strategy costs, operating profit increased \$104 million. Operating margin decreased 20 basis points to 6.2%, while the adjusted operating margin increased 10 basis points to 6.5%.

Operating profit for the Forwarding unit increased \$61 million in 2018 compared with 2017. Excluding the \$16 million impact related to transformation strategy costs, operating profit increased \$77 million. Operating profit and margins increased mainly due to tonnage increases in our international air freight and ocean freight forwarding business as well as pricing improvements. Additionally, our truckload brokerage business grew due to robust demand and tight capacity.

Operating profit for the Logistics unit increased \$12 million in 2018 compared with 2017. Excluding the \$22 million impact related to transformation strategy costs, operating profit increased \$34 million. Operating profit and margins increased due to higher demand in the healthcare, aerospace, retail and manufacturing sectors.

UPS Freight operating profit decreased \$40 million in 2018 compared with 2017. Excluding the \$6 million impact related to transformation strategy costs, operating profit decreased \$34 million. Operating profit and margins decreased as volume declined due to labor uncertainties around the Teamsters contract ratification, partially offsetting the increased LTL revenue per hundredweight realized during the year. Actions to clear our LTL network as a result of the contract ratification process reduced operating profit by approximately \$60 million.



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The combined operating profit for all of our other businesses within Supply Chain & Freight increased \$22 million in 2018, primarily due to higher operating profit at UPS Capital, UPS Customer Solutions and The UPS Store, as well as service contracts with the U.S. Postal Service. Excluding the \$5 million impact related to transformation strategy costs, operating profit increased \$27 million.

2017 compared to 2016

Total operating profit for the Supply Chain & Freight segment increased \$154 million in 2017 compared with 2016. Operating profit for the Forwarding unit increased \$49 million in 2017 compared with 2016. Operating profit and margins for the North American air freight business increased in 2017 due to an increase in volume, slightly offset by higher transportation expenses. Operating profit and margins in our international air freight forwarding business increased due to volume increases and higher revenue per kilo, slightly offset by higher rates at which we procure capacity from third-party air carriers.

Operating profit for the Logistics unit increased \$65 million in 2017 compared to 2016 due to strong performance in the U.S. as well as within our mail services. Additionally, the Marken acquisition in 2016 contributed to the increase in operating profit.

UPS Freight operating profit increased \$7 million in 2017 compared with 2016, as increased volume and prices were partially offset by increased purchased transportation costs.

The combined operating profit for all of our other businesses in this segment increased \$33 million in 2017, primarily due to higher operating profit at UPS Capital, UPS Customer Solutions and The UPS Store, as well as service contracts with the U.S. Postal Service.

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## Consolidated Operating Expenses

	Year Ended December 31,			% Change	
	2018	2017	2016	2018/ 2017	2017/ 2016
Operating Expenses (in millions):					
Compensation and Benefits:	\$37,235	\$34,577	\$32,534	7.7	% 6.3 %
Transformation Strategy Costs	(262 )	—	—		
Adjusted Compensation and Benefits	36,973	34,577	32,534	6.9	% 6.3 %
Repairs and Maintenance	1,732	1,601	1,542	8.2	% 3.8 %
Depreciation and Amortization	2,207	2,282	2,224	(3.3 )	% 2.6 %
Purchased Transportation	13,409	11,696	9,848	14.6	% 18.8%
Fuel	3,427	2,690	2,118	27.4	% 27.0%
Other Occupancy	1,362	1,155	1,037	17.9	% 11.4%
Other Expenses	5,465	5,055	4,619	8.1	% 9.4 %
Total Other Expenses	27,602	24,479	21,388	12.8	% 14.5%
Other Transformation Strategy Costs	(98 )	—	—		
Adjusted Total Other Expenses	\$27,504	\$24,479	\$21,388	12.4	% 14.5%
Total Operating Expenses	\$64,837	\$59,056	\$53,922	9.8	% 9.5 %
Adjusted Total Operating Expenses	\$64,477	\$59,056	\$53,922	9.2	% 9.5 %
Currency Translation Cost / (Benefit)*				\$201	\$62

\* Amount represents the change compared to the prior year.

## Compensation and Benefits

## 2018 compared to 2017

Total compensation and benefits increased \$2.658 billion in 2018 compared to 2017. Excluding the impact of transformation strategy costs of \$262 million discussed in note 16 to the audited consolidated financial statements, adjusted compensation and benefits expense increased \$2.396 billion in 2018.

Employee payroll costs increased \$1.459 billion in 2018 compared with 2017, largely due to higher U.S. domestic hourly and management compensation costs. Total compensation costs increased 6.9%, while consolidated average daily volume growth was 3.2%. U.S. domestic compensation costs for hourly employees increased largely due to higher volume growth, contractual union wage increases, headcount increases, wage rate adjustments for part time workers and a 5.2% increase in average daily union labor hours. Compensation costs for management employees increased primarily due to merit salary increases and growth in the overall size of the workforce.

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Benefits expense increased \$1.199 billion in 2018 compared to 2017. Excluding the impact of transformation strategy costs of \$262 million, benefits costs increased \$937 million in 2018 compared to 2017, primarily due to the following factors:

Health and welfare costs increased \$341 million in 2018 compared to 2017, largely due to increased contributions to multiemployer plans resulting from contractual contribution rate increases and an overall increase in the size of the workforce.

Pension and retirement benefits expense increased \$312 million in 2018 compared to 2017 primarily due to increased expense in UPS sponsored pension plans due to lower discount rates and additional expenses related to multiemployer plan contributions, which were impacted by contractual contribution rate increases and an overall increase in the size of the workforce. These increases were partially offset by lower Pension Benefit Guaranty Corporation premiums due to prior voluntary pension contributions, as well as the amendment of the UPS Retirement Plan in the prior year.

Vacation, holiday, excused absence, payroll tax and other expenses increased \$244 million in 2018 due to salary increases and growth in the overall size of the workforce.

Workers' compensation expense increased \$40 million in 2018 compared to 2017 as we experienced less favorable actuarial adjustments.

2017 compared to 2016

Total compensation and benefits increased \$2.043 billion in 2017 compared to 2016.

Employee payroll costs increased \$1.273 billion in 2017 compared with 2016, largely due to higher U.S. domestic hourly and management compensation costs. Total compensation costs increased 6.4%, while consolidated average daily volume growth was 5.0%. U.S. domestic compensation costs for hourly employees increased largely due to fourth quarter 2017 seasonal staffing increases resulting from 5.4% volume growth, contractual union wage increases, headcount increases, wage rate adjustments for part time workers and a 6.5% increase in average daily union labor hours. Compensation costs for management employees increased primarily due to merit salary increases and growth in the overall size of the workforce.

Benefits expense increased \$770 million in 2017 compared to 2016, primarily due to the following factors:

Pension costs increased \$342 million in 2017 compared to 2016, primarily due to increased expense in UPS sponsored pension plans due to lower discount rates and additional expenses related to multiemployer plan contributions, which were impacted by contractual contribution rate increases and an overall increase in the size of the workforce.

Health and welfare costs increased \$240 million in 2017, largely due to increased contributions to multiemployer plans resulting from contractual contribution rate increases and an overall increase in the size of the workforce.

Vacation, holiday, excused absence, payroll tax and other expenses increased \$251 million in 2017 due to salary increases and growth in the overall size of the workforce.

Workers' compensation expense decreased \$63 million in 2017 as we experienced more favorable actuarial adjustments. This decrease was partially offset by increases in work hours, medical trends and wage increases.

Insurance reserves are established for estimates of the loss that we will ultimately incur on reported workers' compensation claims, as well as estimates of claims that have been incurred but not reported, and take into account a number of factors, including our history of claim losses, payroll growth and the impact of safety improvement initiatives.

Repairs and Maintenance

2018 compared to 2017

The \$131 million increase in repairs and maintenance expense in 2018 was primarily due to maintenance of our transportation equipment and aircraft and routine repairs to buildings and facilities. Building expansions and additions throughout 2018 also contributed to increases in expense.



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2017 compared to 2016

The \$59 million increase in repairs and maintenance expense in 2017 was primarily due to repairs and maintenance of our transportation equipment resulting from growth in the size of our vehicle fleet and routine repairs to buildings and facilities.

Depreciation and Amortization

2018 compared to 2017

We evaluate the useful lives of all our property, plant and equipment based on our usage, maintenance and replacement policies, and taking into account physical and economic factors that may affect the useful lives of the assets. Refer to note 1 in our consolidated financial statements for further description of our policy.

Total depreciation and amortization expense decreased \$75 million in 2018 compared with 2017. The principal components of this change included:

An increase in expense of \$257 million arising from capital investments in several large facilities and other new projects coming into service. This had the effect of decreasing net income by \$205 million or \$0.24 per share on a basic and diluted basis in 2018; and

A decrease in expense of \$286 million resulting from prospective revisions to our estimates of useful lives for building improvements, vehicles and plant equipment as part of our ongoing investment in transformation. This had the effect of increasing net income by \$228 million or \$0.26 per share on a basic and diluted basis.

Combining the impact of the revisions to the estimated useful lives with the impact of the increased capital investments noted above resulted in a net decrease of \$29 million to depreciation expense and an increase to net income of \$23 million or \$0.03 per share on both a basic and diluted basis in 2018.

The changes to the estimated useful lives described above are expected to decrease 2019 depreciation and amortization expense by approximately \$335 million as compared to 2018. However, this will be largely offset by approximately \$330 million of additional depreciation expense related to the addition of numerous facility automation and capacity expansion projects, which are part of our multi-year transformation strategy.

2017 compared to 2016

Depreciation and amortization expense increased \$58 million in 2017 compared with 2016, primarily due to the following factors: (1) depreciation expense on vehicles increased due to an overall increase in the size of our vehicle fleet in our U.S. Domestic Package and UPS Freight operations, (2) depreciation expense for buildings and facilities increased due to the opening of new facilities and facility automation and capacity expansion projects and (3) amortization expense of intangible assets increased in conjunction with the Marken acquisition. These factors were largely offset by a decrease in amortization expense related to longer lived internally developed capitalized software.

Purchased Transportation

2018 compared to 2017

The \$1.713 billion increase in purchased transportation expense charged to us by third-party air, rail, ocean and truck carriers in 2018 compared with 2017 was primarily driven by the following factors:

Expense for our Forwarding and Logistics business increased \$824 million in 2018, primarily due to increased truckload brokerage freight loads per day; increased tonnage in our international air freight forwarding business, and increased volume and rates for mail services. Additionally, expenses increased due to additional fuel surcharges passed onto us from outside contract carriers.

U.S. Domestic Package expense increased \$326 million in 2018, primarily due to increased volume, general rate increases and higher fuel surcharges passed to us from outside contract carriers.

International Package expense increased \$180 million in 2018, primarily due to the increased usage of third-party carriers to handle higher transborder volume and an unfavorable impact from currency exchange rate movements.





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UPS Freight expense increased \$153 million in 2018, due to an increase in our ground freight pricing product, LTL tonnage and higher fuel surcharges passed to us from outside transportation providers, partially offset by declines in our LTL shipments due to fourth quarter labor uncertainties around the Teamsters contract ratification.

We incurred additional purchased transportation expense of \$230 million in 2018 compared to 2017, which was primarily due to leasing additional aircraft to handle increases in air volume and higher jet fuel surcharges associated with aircraft charters.

2017 compared to 2016

The \$1.848 billion increase in purchased transportation expense charged to us by third-party air, rail, ocean and truck carriers in 2017 compared with 2016 was primarily driven by the following factors:

Expense for our Forwarding and Logistics business increased \$937 million in 2017, primarily due to increased truckload brokerage freight loads per day and the resulting increased fuel surcharges passed to us from outside transportation providers; increased volume and rates for mail services; and increased tonnage in our North American and international air freight forwarding businesses. Additionally, purchased transportation expense increased due to the acquisition of Marken in December 2016.

U.S. Domestic Package expense increased \$421 million in 2017, primarily due to increased volume (including SurePost), higher rates and higher fuel surcharges passed to us from outside contract carriers.

International Package expense increased \$270 million in 2017, primarily due to the increased usage of third-party carriers (due to higher volume); higher fuel surcharges passed to us from outside transportation providers and an unfavorable impact of currency exchange rate movements.

UPS Freight expense increased \$163 million in 2017, due to an increase in LTL shipments and higher fuel surcharges passed to us from outside transportation providers.

#### Fuel

2018 compared to 2017

Fuel expense increased \$737 million in 2018 as compared to 2017. The increase in fuel expense in 2018 was primarily due to higher jet fuel, diesel and unleaded gasoline prices and higher consumption due to higher total aircraft block hours and increased Domestic Package delivery miles driven as a result of overall higher volume. These increases were partially offset by the benefit of alternative fuel costs.

The manner in which we purchase fuel also influences the net impact of fuel on our results. The majority of our contracts for fuel purchases utilize index-based pricing formulas plus or minus a fixed locational/supplier differential. While many of the indices are aligned, each index may fluctuate at a different pace, driving variability in the prices paid for fuel. Because of this, our operating results may be affected should the market price of fuel suddenly change by a significant amount or change by amounts that do not result in an adjustment in our fuel surcharges, which can significantly affect our earnings either positively or negatively in the short-term.

2017 compared to 2016

The \$572 million increase in fuel expense in 2017 as compared to 2016 was primarily due to higher jet fuel, diesel and unleaded gasoline prices, which increased fuel expense by \$419 million. Additionally, increased alternative fuel costs and fuel consumption increased expense by \$170 million primarily due to volume increases, which resulted in higher total aircraft block hours and Domestic Package delivery miles driven. These increases were partially offset by increased fuel efficiency.

#### Other Occupancy

2018 compared to 2017

The \$207 million increase in other occupancy expense in 2018 compared to 2017 was largely due to higher facility rent expense, property tax expense and utility expenses. These increases were primarily driven by an increase in the number of operating facilities compared to 2017.



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2017 compared to 2016

The \$118 million increase in other occupancy expense in 2017 compared to 2016 was largely due to higher facility rent expense driven by new facilities, as well as higher utilities and property taxes at our operating facilities.

Other Expenses

2018 compared to 2017

The \$410 million increase in other expenses in 2018 compared to 2017 was primarily attributable to increases in transportation equipment rental, outside professional service costs, security protection, non-income based state and local taxes, and data processing costs. Additionally, costs of \$86 million related to our transformation strategy contributed to the increase in 2018 when compared to 2017.

2017 compared to 2016

The \$436 million increase in other expenses in 2017 compared to 2016 was caused by (1) an auto liability insurance expense increase of \$75 million due to miles driven, medical trend rates and severity experience trends and (2) transportation equipment rental increase of \$60 million driven by growth in package volume.

The remaining \$280 million increase is comprised of increases in several other expense categories, including outside professional services, security protection, computer and plant supplies and air cargo handling, partially offset by a decrease in advertising expense.

Other Income and (Expense)

The following table sets forth investment income (expense) and other and interest expense for the years ended December 31, 2018, 2017 and 2016 (in millions):

	Year Ended December 31,			% Change	
	2018	2017	2016	2018/ 2017	2017/ 2016
Investment Income (Expense) and Other	\$(400 )	61	(2,186 )	NA	(102.8)%
Defined Benefit Plans Mark-to-Market Charges	1,627	800	2,651	103.4%	(69.8 )%
Adjusted Investment Income (Expense) and Other	1,227	861	465	42.5 %	85.2 %
Interest Expense	(605 )	(453 )	(381 )	33.6 %	18.9 %
Total Other Income and (Expense)	\$(1,005)	\$(392)	\$(2,567)	156.4%	(84.7 )%
Adjusted Other Income and (Expense)	\$622	\$408	\$84	52.5 %	NA

Investment Income (Expense) and Other

2018 compared to 2017

Investment income (expense) and other for the period decreased \$461 million, which included a \$827 million increase in mark-to-market pension charges. Excluding the impact of the defined benefit plan mark-to-market charges, adjusted investment income (expense) and other for the period increased \$366 million, which was comprised of expected investment returns on pension assets, net of interest cost on projected benefit obligations and prior service cost.

Expected returns on plan assets increased as a result of both higher discretionary contributions and higher actual returns on plan assets in 2017. Interest cost on projected benefit obligations decreased as a result of lower discount rates. Investment income increased as a result of higher yields on invested assets, partially offset by foreign currency exchange rate movements.

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2017 compared to 2016

Investment income (expense) and other for the period increased \$2.247 billion, which included a \$1.851 billion decrease in mark-to-market pension charges. Excluding the impact of the defined benefit plan mark-to-market charges, adjusted investment income (expense) and other for the period increased \$396 million, which was comprised of expected investment returns on pension assets, net of interest cost on projected benefit obligations and prior service cost. Expected returns on plan assets increased as a result of higher discretionary contributions in 2017 and 2016. Investment income also increased as a result of higher invested assets and the ongoing reduction in losses from fair value adjustments on real estate partnerships, partially offset by foreign currency exchange rate movements.

Interest Expense

2018 compared to 2017

Interest expense increased in 2018 as compared to 2017, primarily due to higher average outstanding debt balances and higher effective interest rates, partially offset by higher capitalized interest related to several large construction projects.

2017 compared to 2016

Interest expense increased in 2017 as compared to 2016, primarily due to the issuance of long-term Canadian Dollar Senior Notes, Euro Senior Notes and U.S. Dollar Senior Notes and higher effective interest rates on senior notes.

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Income Tax Expense

The following table sets forth income tax expense and our effective tax rate for the years ended December 31, 2018, 2017 and 2016 (in millions):

	Year Ended December 31,			% Change	
	2018	2017	2016	2018/ 2017	2017/ 2016
Income Tax Expense:	\$1,228	\$2,232	\$1,699	(45.0)%	31.4%
Income Tax Impact of:					
Defined Benefit Plans Mark-to-Market Charge	390	193	978		
Transformation Strategy Costs	87	—	—		
Income Tax Benefit from the Tax Cuts and Jobs Act and Other	—	258	—		
Non-U.S. Tax Law Changes					
Adjusted Income Tax Expense	\$1,705	\$2,683	\$2,677	(36.5)%	0.2%
Effective Tax Rate	20.4%	31.3%	33.2%		
Adjusted Effective Tax Rate	21.3%	33.8%	34.4%		

Our effective tax rate is affected by recurring factors such as statutory tax rates in the jurisdictions in which we operate and the relative amounts of taxable income we earn in those jurisdictions. It is also affected by discrete items that may occur in any given year but may not be consistent from year to year.

Our effective tax rate decreased to 20.4% in 2018, compared with 31.3% in 2017 and 33.2% in 2016, primarily due to the effects of the aforementioned recurring factors and the following discrete tax items.

Tax Cuts and Jobs Act

On December 22, 2017, the United States enacted into law the Tax Act. The Tax Act made broad and complex changes to the U.S. tax code, including a permanent corporate rate reduction to 21% and a transition to a territorial international system effective in 2018. The Tax Act includes provisions that affected 2017, including: (1) requiring a one-time transition tax on certain unrepatriated earnings of foreign subsidiaries ("Transition Tax") that is payable over eight years; (2) requiring a remeasurement of all U.S. deferred tax assets and liabilities to the newly enacted corporate tax rate of 21% and (3) providing for additional first-year depreciation that allows full expensing of qualified property placed into service after September 27, 2017.

In late December 2017, the SEC staff issued Staff Accounting Bulletin ("SAB") 118, which provided guidance on accounting for the tax effects of the Tax Act. SAB 118 provides a measurement period that should not extend beyond one year from the Tax Act enactment date for companies to complete the related accounting under U.S. GAAP. We recorded a \$272 million provisional benefit inclusive of our Transition Tax liability, the change in our indefinite reinvestment assertion for certain foreign subsidiaries and the remeasurement of our U.S. net deferred tax liabilities for the year ended December 31, 2017. During the fourth quarter of 2018, we completed our accounting for the Tax Act based on the current regulatory guidance available at the end of the SAB 118 measurement period and recorded no net adjustment to our provisional estimate.

The Tax Act also enacted provisions that took effect in 2018 including but not limited to: (1) a provision that imposes U.S. tax on certain foreign subsidiary income known as Global Intangible Low-Taxed Income ("GILTI"); (2) a new deduction for Foreign-Derived Intangible Income ("FDII"); (3) additional limitations on tax deductions for expenses such as interest and executive compensation, and (4) a new minimum tax based on certain payments from a U.S. company to foreign related parties known as the Base Erosion and Anti-Abuse Tax ("BEAT").

We included the impact of each of the newly effective Tax Act provisions in our computation of the 2018 income tax expense. Throughout 2018, the U.S. Department of the Treasury and Internal Revenue Service issued preliminary regulatory guidance clarifying certain provisions of the Tax Act. We anticipate additional regulatory guidance and technical clarifications that could change our future income tax expense. When additional guidance is issued, we will recognize the related tax impact in the quarter of enactment.



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2018 Discrete Items

The decrease in our effective tax rate was primarily due to the impact of the Tax Act which reduced the U.S. federal corporate income tax rate from 35% to 21% effective January 1, 2018.

In the fourth quarter of 2018, we recognized an income tax benefit of \$390 million related to pre-tax mark-to-market losses of \$1.627 billion on our pension and postretirement defined benefit plans. This income tax benefit was generated at a higher average tax rate than the 2018 U.S. federal statutory tax rate because it included the effect of U.S. state and local and foreign taxes.

We recorded pre-tax transformation strategy costs of \$360 million during the year ended December 31, 2018. As a result, we recorded an additional income tax benefit of \$87 million. This income tax benefit was generated at a higher average tax rate than the 2018 U.S. federal statutory tax rate due to the effect of U.S. state and local and foreign taxes. The recognition of excess tax benefits and deficiencies related to share-based compensation in income tax expense resulted in a net tax benefit of \$38 million and reduced our effective tax rate by 0.6% during the year ended December 31, 2018.

Other factors that impacted our 2018 effective tax rate include favorable resolutions of uncertain tax positions, favorable U.S. state and local tax law changes, favorable tax provisions enacted in the Bipartisan Budget Act of 2018 and discrete tax credits associated with the filing of our 2017 U.S. federal income tax return.

2017 Discrete Items

In addition to the impact of the Tax Act described above, the following discrete items were recorded during the year ended December 31, 2017.

In the fourth quarter of 2017, we recognized an income tax benefit of \$193 million related to pre-tax mark-to-market losses of \$800 million on our pension and postretirement defined benefit plans. This income tax benefit was generated at a lower average tax rate than the 2017 U.S. federal statutory tax rate due to future tax rate changes enacted by the Tax Act and differences between U.S. and foreign statutory rates, which was partially offset by the effect of U.S. state and local taxes.

In the fourth quarter of 2017, tax law changes were enacted in certain non-U.S. jurisdictions in which we operate. As a result, we recorded a decrease to our foreign net deferred tax assets of \$14 million with a corresponding net increase to deferred tax expense of \$14 million for the year ended December 31, 2017.

In the first quarter of 2017, we adopted a new accounting standard that requires the recognition of excess tax benefits related to share-based compensation in income tax expense, which resulted in tax benefits for the year ended December 31, 2017 of \$71 million and reduced our effective tax rate by 1.0%.

2016 Discrete Items

In the fourth quarter of 2016, we recognized an income tax benefit of \$978 million related to pre-tax mark-to-market losses of \$2.651 billion on our pension and postretirement defined benefit plans. This income tax benefit was generated at a higher average tax rate than the U.S. federal statutory tax rate because it included the effect of U.S. state and local taxes.

As described in the Items Affecting Comparability section, certain items have been excluded from comparisons of "adjusted" income taxes in the discussion that follows.

Our adjusted effective tax rate decreased to 21.3% in 2018 from 33.8% in 2017 primarily due to the impact of the Tax Act which reduced the U.S. federal corporate income tax rate from 35% to 21% effective January 1, 2018.

Our adjusted effective tax rate decreased to 33.8% in 2017 from 34.4% in 2016 primarily due to favorable discrete tax adjustments related to recognition of excess tax benefits related to share-based compensation in income tax expense.





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Liquidity and Capital Resources

As of December 31, 2018, we had \$5.035 billion in cash, cash equivalents and marketable securities. We believe that our current cash position, access to the commercial paper programs and long-term debt capital markets and cash flow generated from operations should be adequate not only for operating requirements but also to enable us to complete our capital expenditure programs, transformation strategy and to fund dividend payments, share repurchases and long-term debt payments through the next several years. We regularly evaluate opportunities to optimize our capital structure, including through issuances of debt to refinance existing debt and to fund ongoing cash needs.

Cash Flows From Operating Activities

The following is a summary of the significant sources (uses) of cash from operating activities (amounts in millions):

	2018	2017	2016
Net Income	\$4,791	\$4,905	\$3,422
Non-cash operating activities <sup>(1)</sup>	6,048	5,770	6,438
Pension and postretirement plan contributions (UPS sponsored plans)	(186 )	(7,794 )	(2,668 )
Hedge margin receivables and payables	482	(732 )	(142 )
Income tax receivables and payables	469	(550 )	(505 )
Changes in working capital and other non-current assets and liabilities	1,091	(168 )	(47 )
Other operating activities	16	48	(25 )
Net cash from operating activities	\$12,711	\$1,479	\$6,473

(1) Represents depreciation and amortization, gains and losses on derivative transactions and foreign exchange, deferred income taxes, provisions for uncollectible accounts, pension and postretirement benefit expense, stock compensation expense and other non-cash items.

Cash from operating activities remained strong throughout 2016 to 2018. Most of the variability in operating cash flows during the 2016 to 2018 time period relates to the funding of our company-sponsored pension and postretirement benefit plans (and related cash tax deductions). Except for discretionary or accelerated fundings of our plans, contributions to our company-sponsored pension plans have largely varied based on whether any minimum funding requirements are present for individual pension plans. We made no discretionary contributions to our three primary company-sponsored U.S. pension plans in 2018, however we made contributions of \$7.291 and \$2.461 billion in 2017 and 2016, respectively. The remaining contributions from 2016 to 2018 were due to contributions to our international pension plans and U.S. postretirement medical benefit plans.

Apart from the transactions described above, operating cash flow was impacted by changes in our hedge margin receivables and payables, timing of income tax receipts and payments and improvements in our working capital position. The net hedge margin collateral received (paid) from our derivative counterparties was \$482, \$(732) and \$(142) million during 2018, 2017 and 2016, respectively, due to settlements and changes in the fair value of the derivative contracts used in our currency and interest rate hedging programs. Cash payments for income taxes were \$2 million, \$1.559 billion and \$2.064 billion for 2018, 2017 and 2016, respectively, primarily impacted by the timing of a \$5.0 billion pension contribution made in December 2017 which resulted in a tax refund in 2018, and the timing of current tax deductions.

As of December 31, 2018, the total of our worldwide holdings of cash, cash equivalents and marketable securities were \$5.035 billion, of which approximately \$2.853 billion was held by foreign subsidiaries. The amount of cash, cash equivalents and marketable securities held by our U.S. and foreign subsidiaries fluctuates throughout the year due to a variety of factors, including the timing of cash receipts and disbursements in the normal course of business. Cash provided by operating activities in the U.S. continues to be our primary source of funds to finance domestic operating needs, capital expenditures, share repurchases and dividend payments to shareowners. All cash, cash equivalents and marketable securities held by foreign subsidiaries are generally available for distribution to the U.S. without any U.S. federal income taxes. Any such distributions may be subject to foreign withholding and U.S. state taxes. When amounts earned by foreign subsidiaries are expected to be indefinitely reinvested, no accrual for taxes is provided.



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Cash Flows From Investing Activities

Our primary sources (uses) of cash for investing activities were as follows (amounts in millions):

	2018	2017	2016
Net cash used in investing activities	\$(6,330)	\$(4,971)	\$(2,563)
Capital Expenditures:			
Buildings, facilities and plant equipment	\$(3,147)	\$(2,954)	\$(1,316)
Aircraft and parts	(1,496 )	(789 )	(350 )
Vehicles	(931 )	(924 )	(864 )
Information technology	(709 )	(560 )	(435 )
Total Capital Expenditures <sup>(1)</sup>	\$(6,283)	\$(5,227)	\$(2,965)
Capital Expenditures as a % of Revenue	8.7 %	7.9 %	4.9 %
Other Investing Activities:			
Proceeds from disposals of property, plant and equipment	\$37	\$24	\$88
Net decrease in finance receivables	\$4	\$5	\$9
Net (purchases), sales of marketable securities	\$(87 )	\$360	\$911
Cash paid for business acquisitions	\$(2 )	\$(134 )	\$(547 )
Other investing activities	\$1	\$1	\$(59 )

<sup>(1)</sup> In addition to capital expenditures of \$6.283 billion in 2018, there were capital expenditures relating to the principal repayments of capital lease obligations of \$340 million. These are included in cash flows from financing activities.

We have commitments for the purchase of aircraft, vehicles, equipment and real estate to provide for the replacement of existing capacity and anticipated future growth. We generally fund our capital expenditures with our cash from operations. Future capital spending for anticipated growth and replacement assets will depend on a variety of factors, including economic and industry conditions. In 2017 we began a multi-year investment program in our smart logistics network which impacts all asset categories, with the largest investments in buildings, facilities and plant equipment. This investment program will continue in 2019, whereby we anticipate that our capital expenditures will be approximately \$7.0 billion.

As such, capital expenditures on buildings, facilities and plant equipment increased in 2018 compared to prior periods in our U.S. and international package businesses, largely due to several facility automation and capacity expansion projects. Capital spending on aircraft also increased in 2018 compared to prior periods due to increased contract deposits on open aircraft orders and final payments associated with the delivery of aircraft. Capital spending on information technology increased in 2018 compared to the prior periods due to further development of technology enabled enhancements and capitalized software projects.

The proceeds from the disposal of property, plant and equipment were largely due to the disposal of equipment in 2018, vehicle retirements in 2017 and insurance recoveries in 2016. The purchases and sales of marketable securities are largely determined by liquidity needs and the periodic rebalancing of investment types and will fluctuate from period to period.

Cash paid for business acquisitions was related to our acquisition of area franchise rights for The UPS Store in 2018, Freightex, Nightline and STTAS in 2017 and Marken in 2016.

Other investing activities are impacted by changes in our non-current investments, capital contributions into certain investment partnerships and various other items.

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Cash Flows From Financing Activities

Our primary sources (uses) of cash for financing activities were as follows (amounts in millions, except per share data):

	2018	2017	2016
Net cash used in financing activities	\$(5,692 )	\$3,287	\$(3,140 )
Share Repurchases:			
Cash expended for shares repurchased	\$(1,011 )	\$(1,813 )	\$(2,678 )
Number of shares repurchased	(8.9 )	(16.1 )	(25.4 )
Shares outstanding at year-end	858	859	868
Percent reduction in shares outstanding	(0.1 )%	(1.0 )%	(2.0 )%
Dividends:			
Dividends declared per share	\$3.64	\$3.32	\$3.12
Cash expended for dividend payments	\$(3,011 )	\$(2,771 )	\$(2,643 )
Borrowings:			
Net borrowings (repayments) of debt principal	\$(1,622 )	\$7,827	\$2,034
Other Financing Activities:			
Cash received for common stock issuances	\$240	\$247	\$245
Other financing activities	\$(288 )	\$(203 )	\$(98 )
Capitalization:			
Total debt outstanding at year-end	\$22,736	\$24,289	\$16,075
Total shareowners' equity at year-end	3,037	1,024	430
Total capitalization	\$25,773	\$25,313	\$16,505

For the years ended December 31, 2018, 2017 and 2016, we repurchased a total of 8.9, 16.1 and 25.2 million shares of class A and class B common stock for \$1.000, \$1.816 and \$2.680 billion, respectively (\$1.011, \$1.813 and \$2.678 billion in repurchases for 2018, 2017 and 2016, respectively, are reported on the cash flow statement due to the timing of settlements).

In May 2016, the Board of Directors approved a share repurchase authorization of \$8.0 billion, which replaced an authorization previously announced in 2013. The share repurchase authorization has no expiration date. As of December 31, 2018, we had \$3.339 billion of this share repurchase authorization remaining.

Share repurchases may take the form of accelerated share repurchases, open market purchases, or other such methods as we deem appropriate. The timing of our share repurchases will depend upon market conditions. We anticipate repurchasing approximately \$1.0 billion of shares in 2019.

The declaration of dividends is subject to the discretion of the Board of Directors and will depend on various factors, including our net income, financial condition, cash requirements, future prospects and other relevant factors. We expect to continue the practice of paying regular cash dividends. In February 2019, we increased our quarterly dividend payment from \$0.91 to \$0.96 per share, a 5.5% increase.

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Issuances of debt in 2018 consisted primarily of commercial paper. In 2017 and 2016 we completed senior rate note offerings of \$8.355 and \$1.775 billion, respectively. The following is a summary of debt issuances in 2017 and 2016 (in millions):

	Principal Amount in USD
2017	
Fixed-rate senior notes:	
2.050% senior notes	\$ 700
2.350% senior notes	600
2.500% senior notes	1,000
2.800% senior notes	500
3.050% senior notes	1,000
3.750% senior notes	1,150
Floating-rate senior notes (multiple issuances)	1,461
Euro senior notes:	
0.375% senior notes (€700)	815
1.500% senior notes (€500)	582
Canadian senior notes:	
2.125% senior notes (C\$750)	547
Total	\$ 8,355
	Principal Amount in USD
2016	
Fixed-rate senior notes:	
2.400% senior notes	\$ 500
3.400% senior notes	500
Floating-rate senior notes (multiple issuances)	226
Euro senior notes:	
1.000% senior notes (€500)	549
	\$ 1,775

The remaining debt issuances for 2017 and 2016 consisted primarily of commercial paper.

Repayment of debt in 2018 and 2017 consisted primarily of the maturity of our \$750 million 5.50% fixed-rate senior notes that matured in January 2018 and \$375 million 1.125% fixed-rate senior notes that matured in October 2017. In 2016, there were no repayments of fixed-rate senior notes or floating-rate senior notes. The remaining repayments of debt during the 2016 through 2018 time period included paydowns of commercial paper and scheduled principal payments on our capitalized lease obligations. We consider the overall fixed and floating interest rate mix of our portfolio and the related overall cost of borrowing when planning for future issuances and non-scheduled repayments of debt.

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The amount of commercial paper outstanding fluctuates throughout the year based on daily liquidity needs. The following is a summary of our commercial paper program (amount in millions):

Functional currency outstanding balance at year-end	Outstanding balance at year-end (\$)	Average balance outstanding	Average balance outstanding (\$)	Average interest rate
2018				
USD \$ 1,968	\$ 1,968	\$ 2,137	\$ 2,137	1.81 %
EUR € 606	\$ 694	€ 360	\$ 425	(0.38)%
Total	\$ 2,662			

Functional currency outstanding balance at year-end	Outstanding balance at year-end (\$)	Average balance outstanding	Average balance outstanding (\$)	Average interest rate
2017				
USD \$ 2,458	\$ 2,458	\$ 2,163	\$ 2,163	0.88 %
EUR € 622	\$ 745	€ 941	\$ 1,062	(0.39)%
Total	\$ 3,203			

Functional currency outstanding balance at year-end	Outstanding balance at year-end (\$)	Average balance outstanding	Average balance outstanding (\$)	Average interest rate
2016				
USD \$ 2,406	\$ 2,406	\$ 1,838	\$ 1,838	0.44 %
EUR € 801	\$ 844	€ 776	\$ 817	(0.28)%
GBP £ —	\$ —	£ 94	\$ 116	0.50 %
Total	\$ 3,250			

The variation in cash received from common stock issuances was primarily due to the level of stock option exercises by employees in the 2016 through 2018 period.

The cash outflows in other financing activities were impacted by several factors, primarily the repurchase of shares to satisfy tax withholding obligations on vested employee stock awards of \$259, \$247 and \$167 million for 2018, 2017 and 2016, respectively. Net cash inflows from premium received on capped call options for the purchase of UPS class B shares were \$34 million in 2018, and \$54 million in both 2017 and 2016.

#### Sources of Credit

See note 8 to the audited consolidated financial statements for a discussion of our available credit and debt covenants.

#### Guarantees and Other Off-Balance Sheet Arrangements

We do not have guarantees or other off-balance sheet financing arrangements, including variable interest entities, which we believe could have a material impact on financial condition or liquidity.

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Contractual Commitments

We have contractual obligations and commitments in the form of capital leases, operating leases, debt obligations, purchase commitments and certain other liabilities. We intend to satisfy these obligations through the use of cash flow from operations. The following table summarizes the expected cash outflow to satisfy our contractual obligations and commitments as of December 31, 2018 (in millions):

Commitment Type	2019	2020	2021	2022	2023	After 2023	Total
Capital Leases	\$158	\$95	\$42	\$39	\$36	\$293	\$663
Operating Leases	578	477	399	325	262	926	2,967
Debt Principal	3,667	998	2,551	2,000	2,303	10,830	22,349
Debt Interest	624	582	525	461	389	5,626	8,207
Purchase Commitments <sup>(1)</sup>	3,686	1,732	1,150	383	22	8	6,981
Tax Act Repatriation Liability	—	—	—	—	—	96	96
Pension Funding	2,192	—	—	—	—	—	2,192
Total	\$10,905	\$3,884	\$4,667	\$3,208	\$3,012	\$17,779	\$43,455

<sup>(1)</sup> Purchase commitments include aircraft leases that we entered into in 2019.

Our capital lease obligations relate primarily to leases on aircraft and real estate. Capital leases, operating leases and purchase commitments, as well as our debt principal obligations, are discussed further in note 8 to our consolidated financial statements. The amount of interest on our debt was calculated as the contractual interest payments due on our fixed-rate debt, in addition to interest on variable rate debt that was calculated based on interest rates as of December 31, 2018. The calculations of debt interest take into account the effect of interest rate swap agreements. For debt denominated in a foreign currency, the U.S. Dollar equivalent principal amount of the debt at the end of the year was used as the basis to calculate future interest payments.

Purchase commitments represent contractual agreements to purchase assets, goods or services that are legally binding, including contracts for aircraft, construction of new or expanded facilities and orders for technology equipment and vehicles. As of December 31, 2018, we had firm commitments to purchase 19 new Boeing 747-8F cargo aircraft to be delivered between 2019 and 2022 and nine Boeing 767 aircraft to be delivered between 2019 and 2020.

On December 22, 2017, the United States enacted into law the Tax Act requiring a one-time transition tax on certain unrepatriated earnings of foreign subsidiaries. Companies may elect to pay the tax over eight years based on an installment schedule outlined in the Tax Act but are required under current IRS guidance to offset certain overpayments of tax against the liability. We intend to make this election and have reflected our remaining transition tax due by year as a contractual obligation.

There are no anticipated required minimum cash contributions to our qualified U.S. pension plans in 2019 (these plans are discussed further in note 5 to the audited consolidated financial statements). The amount of any minimum funding requirement, as applicable, for these plans could change significantly in future periods, depending on many factors, including future plan asset returns, discount rates and changes to pension plan funding regulations. A decline in discount rates or a sustained significant decline in the world equity or bond markets could result in our domestic pension plans being subject to significantly higher minimum funding requirements. Actual contributions made in future years could materially differ and consequently required minimum contributions beyond 2019 cannot be reasonably estimated.

As discussed in note 6 to the audited consolidated financial statements, we are not currently subject to any minimum contributions or surcharges with respect to the multiemployer pension and health and welfare plans in which we participate. Contribution rates to these multiemployer pension and health and welfare plans are established through the collective bargaining process. As we are not subject to any minimum contribution levels, we have not included any amounts in the contractual commitments table with respect to these multiemployer plans.



The table above does not include approximately \$216 million of liabilities for uncertain tax positions because we are uncertain if or when such amounts will ultimately be settled in cash. Uncertain tax positions are further discussed in note 13 to the consolidated financial statements.

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As of December 31, 2018, we had outstanding letters of credit totaling approximately \$1.256 billion issued in connection with our self-insurance reserves and other routine business requirements. We also issue surety bonds as an alternative to letters of credit in certain instances, and as of December 31, 2018, we had \$1.031 million of surety bonds written. As of December 31, 2018, we had unfunded loan commitments totaling \$164 million associated with UPS Capital.

We believe that funds from operations and borrowing programs will provide adequate sources of liquidity and capital resources to meet our expected long-term needs for the operation of our business, including anticipated capital expenditures, for the foreseeable future.

#### Contingencies

See note 5 to the audited consolidated financial statements for a discussion of pension related matters and note 9 for a discussion of judicial proceedings and other matters arising from the conduct of our business activities.

#### Collective Bargaining Agreements

##### Status of Collective Bargaining Agreements

As of December 31, 2018, we had approximately 283,000 employees employed under a national master agreement and various supplemental agreements with local unions affiliated with the Teamsters. These agreements expired on July 31, 2018. On October 5, 2018, the Teamsters declared that the tentative national master agreement for the U.S. Domestic Package business unit was considered ratified, and will be implemented as soon as five remaining local and supplemental agreements are negotiated and ratified. We remain in the process of negotiating and ratifying four of these local and supplemental agreements which, when ratified, will be retroactive to August 1, 2018. The UPS Freight business unit national master agreement was ratified on November 11, 2018.

We have approximately 2,800 pilots who are employed under a collective bargaining agreement with the Independent Pilots Association ("IPA"), which becomes amendable on September 1, 2021.

Our airline mechanics are covered by a collective bargaining agreement with Teamsters Local 2727. On February 8, 2019, the airline mechanics who are covered by this agreement voted to ratify a new contract which will become amendable November 1, 2023. In addition, approximately 3,100 of our auto and maintenance mechanics who are not employed under agreements with the Teamsters are employed under collective bargaining agreements with the International Association of Machinists and Aerospace Workers ("IAM") that will expire on July 31, 2019.

#### Multiemployer Benefit Plans

We contribute to a number of multiemployer defined benefit and health and welfare plans under terms of collective bargaining agreements that cover our union represented employees. Our current collective bargaining agreements set forth the annual contribution increases allotted to the plans that we participate in, and we are in compliance with these contribution rates. These limitations will remain in effect throughout the terms of the existing collective bargaining agreements.

#### New Accounting Pronouncements

##### Recently Adopted Accounting Standards

See note 1 to the audited consolidated financial statements for a discussion of recently adopted accounting standards.

##### Accounting Standards Issued But Not Yet Effective

See note 1 to the audited consolidated financial statements for a discussion of accounting standards issued, but not yet effective.

#### Rate Adjustments

Effective February 18, 2019, general UPS Freight rates will increase by 5.9%. This rate adjustment applies to non-contractual less-than-truckload (LTL) shipments. The impact of this general rate increase may vary by specific lane or shipment characteristics such as weight or class.



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Critical Accounting Policies and Estimates

Our discussion and analysis of our financial condition and results of operations are based on our consolidated financial statements, which are prepared in accordance with accounting principles generally accepted in the United States of America. As indicated in note 1 to our consolidated financial statements, the amounts of assets, liabilities, revenue and expenses reported in our financial statements are affected by estimates and judgments that are necessary to comply with generally accepted accounting principles. We base our estimates on prior experience and other assumptions that we consider reasonable to our circumstances. Actual results could differ from our estimates, which would affect the related amounts reported in our consolidated financial statements. While estimates and judgments are applied in arriving at many reported amounts, we believe that the following matters may involve a higher degree of judgment and complexity.

Contingencies

As discussed in note 9 to the audited consolidated financial statements, we are involved in various legal proceedings and contingencies. The events that may impact our contingent liabilities are often unique and generally are not predictable. At the time a contingency is identified, we consider all relevant facts as part of our evaluation. We record a liability for a loss when the loss is probable of occurring and reasonably estimable. Events may arise that were not anticipated and the outcome of a contingency may result in a loss to us that differs from our previously estimated liability. These factors could result in a material difference between estimated and actual operating results. Contingent losses that are probable and estimable, excluding those related to income taxes and self-insurance which are discussed further below, were not material to our financial position or results of operations as of, and for the year ended, December 31, 2018. In addition, we have certain contingent liabilities that have not been recognized as of December 31, 2018, because a loss is not reasonably estimable.

Goodwill and Intangible Impairment

We perform impairment testing of goodwill for each of our reporting units on an annual basis. In our U.S. Domestic Package and International Package reporting segments, we have the following reporting units: Europe, Asia, Americas and ISMEA (Indian Subcontinent, Middle East and Africa). In our Supply Chain & Freight segment we have the following reporting units: Forwarding, Logistics, UPS Mail Innovations, UPS Freight, The UPS Store, UPS Capital, Marken and Coyote Logistics. Our annual goodwill impairment testing date is July 1<sup>st</sup> for each reporting unit owned at the testing date. In assessing goodwill for impairment, we initially evaluate qualitative factors to determine if it is more likely than not that the fair value of a reporting unit is less than its carrying amount. If the qualitative assessment is not conclusive and it is necessary to calculate the fair value of a reporting unit, then we utilize a two-step process to test goodwill for impairment. First, a comparison of the fair value of the applicable reporting unit with the aggregate carrying value, including goodwill, is performed. If the carrying amount of a reporting unit exceeds the reporting unit's fair value, we perform the second step of the goodwill impairment test to determine the amount of impairment loss. The second step includes comparing the implied fair value of the affected reporting unit's goodwill with the carrying value of that goodwill.

We primarily determine the fair value of our reporting units using a discounted cash flow model ("DCF model") and supplement this with observable valuation multiples for comparable companies, as appropriate. The completion of the DCF model requires that we make a number of significant assumptions to produce an estimate of future cash flows. These assumptions include projections of future revenue, costs, capital expenditures and working capital changes. In addition, we make assumptions about the estimated cost of capital and other relevant variables, as required, in estimating the fair value of our reporting units. The projections that we use in our DCF model are updated annually and will change over time based on the historical performance and changing business conditions for each of our reporting units. The determination of whether goodwill is impaired involves a significant level of judgment in these assumptions, and changes in our business strategy, government regulations, or economic or market conditions could significantly impact these judgments. We routinely monitor market conditions and other factors to determine if interim impairment tests are necessary. If impairment indicators are present in future periods, the resulting impairment

charges could have a material impact on our results of operations.

None of the reporting units incurred any goodwill impairment charges in 2018, 2017 or 2016. Changes in our forecasts could cause carrying values of our reporting units to exceed their fair values in future periods, potentially resulting in a goodwill impairment charge. During the year, management monitored the actual performance of the business relative to the fair value assumptions used during our annual goodwill impairment test. For the periods presented, no triggering events were identified that required an interim impairment test. Based on most recent tests, the fair value of all our reporting units substantially exceed their carrying value.

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A trade name with a carrying value of \$200 million and licenses with a carrying value of \$5 million as of December 31, 2018 are considered to be indefinite-lived intangibles, and therefore are not amortized. Impairment tests for indefinite-lived intangibles are performed on an annual basis. We determined that the income approach, specifically the relief from royalty method, is the most appropriate valuation method for the trade name. The estimated fair value of the trade name is compared to the carrying value of the asset. If the carrying value of the trade name exceeds its estimated fair value, an impairment charge is recognized for the amount by which the carrying amount of the asset exceeds its fair value. This valuation approach requires that we make a number of assumptions to estimate fair value. These assumptions include projections of future revenues, market royalty rates, tax rates, discount rates and other relevant variables. The projections we use in the model are updated annually and will change over time based on the historical performance and changing business conditions.

All of our remaining recorded intangible assets are deemed to be finite-lived intangibles, and are amortized over their estimated useful lives. Impairment tests for these intangible assets are only performed when a triggering event occurs that indicates that the carrying value of the intangible may not be recoverable based on the undiscounted future cash flows of the intangible. If the carrying amount of the intangible is determined not to be recoverable, a write-down to fair value is recorded. Fair values are determined based on a DCF model. If impairment indicators are present in future periods, the resulting impairment charges could have a material impact on our results of operations. There was a \$12 and \$7 impairment of finite-lived intangible assets in 2018 and 2017, respectively and no impairment of finite-lived intangible assets in 2016. There was no impairment of indefinite-lived intangible assets in 2018, 2017 or 2016.

Self-Insurance Accruals

We self-insure costs associated with workers' compensation claims, automobile liability, health and welfare and general business liabilities, up to certain limits. Insurance reserves are established for estimates of the loss that we will ultimately incur on reported claims, as well as estimates of claims that have been incurred but not yet reported. Recorded balances are based on reserve levels, which incorporate historical loss experience and judgments about the present and expected levels of cost per claim. Trends in actual experience are a significant factor in the determination of such reserves. We believe our estimated reserves for such claims are adequate, but actual experience in claim frequency and/or severity could materially differ from our estimates and affect our results of operations.

Workers' compensation, automobile liability and general liability insurance claims may take several years to completely settle. Consequently, actuarial estimates are required to project the ultimate cost that will be incurred to fully resolve the claims. A number of factors can affect the actual cost of a claim, including the length of time the claim remains open, trends in healthcare costs and the results of related litigation. Furthermore, claims may emerge in future years for events that occurred in a prior year at a rate that differs from previous actuarial projections. Changes in state legislation with respect to workers' compensation can affect the adequacy of our self-insurance accruals. All of these factors can result in revisions to prior actuarial projections and produce a material difference between estimated and actual operating results. Prior to 2017, outside actuarial studies were performed semi-annually and we used the studies to estimate the liability in intervening quarters. Beginning in 2017, outside actuarial studies are now performed quarterly as we believe this provides us with better quarterly estimates of our outstanding workers' compensation liability.

We sponsor a number of health and welfare insurance plans for our employees. These liabilities and related expenses are based on estimates of the number of employees and eligible dependents covered under the plans, anticipated medical usage by participants and overall trends in medical costs and inflation. Actual experience may differ from these estimates and, therefore, produce a material difference between estimated and actual operating results.

Pension and Postretirement Medical Benefits

Our pension and other postretirement benefit costs are calculated using various actuarial assumptions and methodologies. These assumptions include discount rates, healthcare cost trend rates, inflation, compensation increase rates, expected returns on plan assets, mortality rates and other factors. The assumptions utilized in recording the obligations under our plans represent our best estimates, and we believe that they are reasonable, based on information as to historical experience and performance as well as other factors that might cause future expectations to differ from past trends.

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Differences in actual experience or changes in assumptions may affect our pension and other postretirement obligations and future expense. The primary factors contributing to actuarial gains and losses each year are (1) changes in the discount rate used to value pension and postretirement benefit obligations as of the measurement date, (2) differences between the expected and the actual return on plan assets, (3) changes in demographic assumptions including mortality, (4) participant experience different from demographic assumptions and (5) changes in coordinating benefits with plans not sponsored by UPS.

We recognize changes in the fair value of plan assets and net actuarial gains or losses in excess of a corridor (defined as 10% of the greater of the fair value of plan assets or the plans' projected benefit obligations) in pension expense annually at December 31st each year. The remaining components of pension expense (herein referred to as "ongoing net periodic benefit cost"), primarily service and interest costs and the expected return on plan assets, are reported on a quarterly basis.

The following sensitivity analysis shows the impact of a 25 basis point change in the assumed discount rate and return on assets for our pension and postretirement benefit plans, and the resulting increase/(decrease) on our obligations and expense as of, and for the year ended, December 31, 2018 (in millions).

Pension Plans	25 Basis Point Increase	25 Basis Point Decrease
Discount Rate:		
Effect on ongoing net periodic benefit cost	\$ (48 )	\$ 50
Effect on net periodic benefit cost for amounts recognized outside the 10% corridor	(360 )	1,065
Effect on projected benefit obligation	(1,717 )	1,823
Return on Assets:		
Effect on ongoing net periodic benefit cost <sup>(1)</sup>	(106 )	106
Effect on net periodic benefit cost for amounts recognized outside the 10% corridor <sup>(2)</sup>	(24 )	24
Postretirement Medical Plans		
Discount Rate:		
Effect on ongoing net periodic benefit cost	3	(3 )
Effect on net periodic benefit cost for amounts recognized outside the 10% corridor	(10 )	11
Effect on accumulated postretirement benefit obligation	(53 )	62
Healthcare Cost Trend Rate:		
Effect on ongoing net periodic benefit cost	1	(1 )
Effect on net periodic benefit cost for amounts recognized outside the 10% corridor	9	(9 )
Effect on accumulated postretirement benefit obligation	15	(16 )

<sup>(1)</sup> Amount calculated based on 25 basis point increase / decrease in the expected return on assets.

<sup>(2)</sup> Amount calculated based on 25 basis point increase / decrease in the actual return on assets.

#### Pension Backstop

UPS was a contributing employer to the Central States Pension Fund ("CSPF") until 2007 when we withdrew from the CSPF and fully funded our allocable share of unfunded vested benefits by paying a \$6.1 billion withdrawal liability. Under a collective bargaining agreement with the International Brotherhood of Teamsters ("IBT"), UPS agreed to provide coordinating benefits in the UPS/IBT Full Time Employee Pension Plan ("UPS/IBT Plan") for UPS participants whose last employer was UPS and who had not retired as of January 1, 2008 ("the UPS Transfer Group") in the event that benefits are lawfully reduced by the CSPF in the future consistent with the terms of our withdrawal agreement with the CSPF. Under our withdrawal agreement with the CSPF, benefits to the UPS Transfer Group cannot be



reduced without our consent and can only be reduced in accordance with applicable law.

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In December 2014, Congress passed the Multiemployer Pension Reform Act (“MPRA”). This change in law for the first time permitted multiemployer pension plans to reduce benefit payments to retirees, subject to specific guidelines in the statute and government approval. In September 2015, the CSPF submitted a proposed pension benefit reduction plan to the U.S. Department of the Treasury (“Treasury”). In May 2016, Treasury rejected the proposed plan submitted by the CSPF. In the first quarter of 2018, Congress established a Joint Select Committee to develop a recommendation to improve the solvency of multiemployer plans and the Pension Benefit Guaranty Corporation (“PBGC”) before a November 30, 2018 deadline. While the Committee’s efforts failed to meet its deadline, the Committee made significant progress towards finding solutions that will address the long term solvency of multiemployer pension plans. UPS will continue to work with all stakeholders, including legislators and regulators, to implement an acceptable solution.

The CSPF has said that it believes a legislative solution to its funded status is necessary or that it will become insolvent in 2025, and we expect that the CSPF will continue to explore options to avoid insolvency. Numerous factors could affect the CSPF’s funded status and UPS’s potential obligation to pay coordinating benefits under the UPS/IBT Plan. Any obligation to pay coordinating benefits will be subject to a number of significant uncertainties, including whether the CSPF submits a revised MPRA filing and the terms thereof, or whether it otherwise seeks federal government assistance, as well as the terms of any applicable legislation, the extent to which benefits are paid by the PBGC and our ability to successfully defend legal positions we may take in the future under the MPRA, including the suspension ordering provisions, our withdrawal agreement and other applicable law.

We account for the potential obligation to pay coordinating benefits to the UPS Transfer Group under Accounting Standards Codification Topic 715- Compensation- Retirement Benefits (“ASC 715”), which requires us to provide a best estimate of various actuarial assumptions, including the eventual outcome of this matter, in measuring our pension benefit obligation at the December 31st measurement date. While we currently believe the most likely outcome to this matter and the broader systemic problems facing multiemployer pension plans is intervention by the federal government, ASC 715 does not permit anticipation of changes in law in making a best estimate of pension liabilities.

As such, our best estimate of the next most likely outcome at the measurement date is that the CSPF submits and implements another benefit reduction plan under the MPRA during 2019. We believe any MPRA filing would be designed to forestall insolvency by reducing benefits to participants other than the UPS Transfer Group to the maximum extent permitted, and then reducing benefits to the UPS Transfer Group by a lesser amount.

We have evaluated this outcome using a deterministic cash flow projection, reflecting updated estimated CSPF cash flows and investment earnings, the lack of legislative action and the absence of a MPRA filing by the CSPF in 2018. As a result, at the December 31, 2018 measurement date, the best estimate of our projected benefit obligation increased by \$1.6 billion for coordinating benefits that may be required to be directly provided by the UPS/IBT Plan to the UPS Transfer Group.

The future value of this estimate will be influenced by the terms and timing of any MPRA filing, changes in our discount rate, rate of return on assets and other actuarial assumptions, presumed solvency of the PBGC, as well as potential solutions resulting from federal government intervention. Any such event may result in a decrease or an increase in the best estimate of our projected benefit obligation. If the uncertainties are not resolved, it is reasonably possible that our projected benefit obligation could increase by approximately \$2.4 billion, resulting in a total obligation for coordinating benefits of approximately \$4.0 billion as previously disclosed. If a future change in law occurs, it may be a significant event requiring an interim remeasurement of the UPS/IBT Plan at the date the law is enacted. We will continue to assess the impact of these uncertainties on our projected benefit obligation in accordance with ASC 715.



UNITED PARCEL SERVICE, INC. AND SUBSIDIARIES  
MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND  
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Depreciation, Residual Value and Impairment of Fixed Assets

As of December 31, 2018, we had \$26.576 billion of net fixed assets, the most significant category of which is aircraft. In accounting for fixed assets, we make estimates about the expected useful lives and the expected residual values of the assets, and the potential for impairment based on the fair values of the assets and the cash flows generated by these assets.

We evaluate the useful lives of our property, plant and equipment based on our usage, maintenance and replacement policies, and taking into account physical and economic factors that may affect the useful lives of the assets. As part of our ongoing investment in transformation in 2018, we revised our estimates of useful lives for building improvements, vehicles and plant equipment based on our current assessment of these factors. In general, these changes in estimate had the effect of lengthening the useful lives of vehicles, building improvements and plant equipment. The change in estimates for building improvements, vehicles and plant equipment was applied prospectively beginning in 2018 through depreciation expense. See "Consolidated Operating Expense" of Item 7 "Management's Discussion and Analysis of Financial Condition and Results of Operations" for the discussion of the impacts to "Depreciation and amortization." See note 1 to the audited consolidated financial statements for a discussion of our accounting policies. See note 4 to the audited consolidated financial statements for a discussion of the change in estimated useful lives.

In estimating the lives and expected residual values of aircraft, we have relied upon actual experience with the same or similar aircraft types. Subsequent revisions to these estimates could be caused by changes to our maintenance program, changes in the utilization of the aircraft, governmental regulations on aging aircraft and changing market prices of new and used aircraft of the same or similar types. We periodically evaluate these estimates and assumptions, and adjust the estimates and assumptions as necessary. Adjustments to the expected lives and residual values are accounted for on a prospective basis through depreciation expense. In estimating cash flows, we project future volume levels for our different air express products in all geographic regions in which we do business. Adverse changes in these volume forecasts, or a shortfall of our actual volume compared with our projections, could result in our current aircraft capacity exceeding current or projected demand. This situation could lead to an excess of a particular aircraft, resulting in an aircraft impairment charge or a reduction of the expected life of an aircraft (thus resulting in increased depreciation expense).

We review long-lived assets for impairment when circumstances indicate the carrying amount of an asset may not be recoverable based on the undiscounted future cash flows of the asset. If the carrying amount of the asset is determined not to be recoverable, a write-down to fair value is recorded. Fair values are determined based on quoted market values, discounted cash flows or external appraisals, as appropriate. We review long-lived assets for impairment at the individual asset or the asset group level for which the lowest level of independent cash flows can be identified. The circumstances that would indicate potential impairment may include, but are not limited to, a significant change in the extent to which an asset is utilized and operating or cash flow losses associated with the use of the asset.

There were no impairment charges on our property, plant and equipment during 2018, 2017 and 2016.

Fair Value Measurements

In the normal course of business, we hold and issue financial instruments that contain elements of market risk, including derivatives, marketable securities, finance receivables, pension assets, other investments and debt. Certain of these financial instruments are required to be recorded at fair value, principally derivatives, marketable securities, pension assets and certain other investments. Fair values are based on listed market prices, when such prices are available. To the extent that listed market prices are not available, fair value is determined based on other relevant factors, including dealer price quotations. If listed market prices and other relevant facts are not available, inputs are developed from unobservable data reflecting our own assumptions and include situations where there is little or no market activity for the asset or liability. Certain financial instruments, including over-the-counter derivative instruments, are valued using pricing models that consider, among other factors, contractual and market prices, correlations, time value, credit spreads and yield curve volatility factors. Changes in the fixed income, foreign

exchange and commodity markets will impact our estimates of fair value in the future, potentially affecting our results of operations. A quantitative sensitivity analysis of our exposure to changes in commodity prices, foreign currency exchange rates and interest rates is presented in the “Quantitative and Qualitative Disclosures about Market Risk” section of this report.

Certain non-financial assets and liabilities are measured at fair value on a nonrecurring basis, including property, plant, and equipment, goodwill and intangible assets. These assets are not measured at fair value on a recurring basis; however, they are subject to fair value adjustments in certain circumstances, such as when there is evidence of an impairment.

UNITED PARCEL SERVICE, INC. AND SUBSIDIARIES  
MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND  
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We allocate the fair value of purchase consideration to the tangible assets acquired, liabilities assumed and intangible assets acquired based on their estimated fair values. The excess of the fair value of purchase consideration over the fair values of these identifiable assets and liabilities is recorded as goodwill. Such valuations require management to make significant estimates and assumptions, especially with respect to intangible assets. Significant estimates in valuing certain intangible assets include, but are not limited to, future expected cash flows from acquired customers, technology and trade names from a market participant perspective, useful lives and discount rates. Management's estimates of fair value are based upon assumptions believed to be reasonable, but which are inherently uncertain and unpredictable and, as a result, actual results may differ from estimates. During the measurement period, which is one year from the acquisition date, we may record adjustments to the assets acquired and liabilities assumed, with the corresponding offset to goodwill. Upon the conclusion of the measurement period, any subsequent adjustments are recorded to earnings.

Income Taxes

We make certain estimates and judgments in determining income tax expense for financial statement purposes. These estimates and judgments occur in the calculation of income by legal entity and jurisdiction, tax credits, benefits, and deductions, and in the calculation of deferred tax assets and liabilities, which arise from differences in the timing of recognition of revenue and expense for tax and financial statement purposes, as well as tax, interest and penalties related to uncertain tax positions. Significant changes to these estimates may result in an increase or decrease to our tax provision in a subsequent period.

We assess the likelihood that we will be able to recover our deferred tax assets. If recovery is not likely, we must increase our provision for taxes by recording a valuation allowance against the deferred tax assets that we estimate will not ultimately be recoverable. We believe that we will ultimately recover a substantial majority of the deferred tax assets recorded on our consolidated balance sheets. However, should there be a change in our ability to recover our deferred tax assets, our tax provision would increase in the period in which we determined that the recovery was not likely.

The calculation of our tax liabilities involves dealing with uncertainties in the application of complex tax regulations. We recognize liabilities for uncertain tax positions based on a two-step process. The first step is to evaluate the tax position for recognition by determining if the weight of available evidence indicates that it is more likely than not that the position will be sustained on audit, including resolution of related appeals or litigation processes, if any. Once it is determined that the position meets the recognition threshold, the second step requires us to estimate and measure the largest amount of tax benefit that is more likely than not to be realized upon ultimate settlement. The difference between the amount of recognizable tax benefit and the total amount of tax benefit from positions filed or to be filed with the tax authorities is recorded as a liability for uncertain tax benefits. It is inherently difficult and subjective to estimate such amounts, as we have to determine the probability of various possible outcomes. We reevaluate uncertain tax positions on a quarterly basis. This evaluation is based on factors including, but not limited to, changes in facts or circumstances, changes in tax law, effectively settled issues under audit, and new audit activity. Such a change in recognition or measurement could result in the recognition of a tax benefit or an additional charge to the tax provision. See note 13 to the audited consolidated financial statements for a discussion of impacts of the Tax Act.

UNITED PARCEL SERVICE, INC. AND SUBSIDIARIES  
MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND  
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Item 7A. Quantitative and Qualitative Disclosures about Market Risk

We are exposed to market risk from changes in certain commodity prices, foreign currency exchange rates and interest rates. All of these market risks arise in the normal course of business, as we do not engage in speculative trading activities. In order to manage the risk arising from these exposures, we utilize a variety of commodity, foreign exchange and interest rate forward contracts, options and swaps. A discussion of our accounting policies for derivative instruments and further disclosures are provided in note 15 to the consolidated financial statements.

Commodity Price Risk

We are exposed to changes in the prices of refined fuels, principally jet-A, diesel and unleaded gasoline, as well as changes in the price of natural gas and other alternative fuels. Currently, the fuel surcharges that we apply to our domestic and international package and LTL services are the primary means of reducing the risk of adverse fuel price changes. In order to mitigate the impact of fuel surcharges imposed on us by outside carriers, we regularly adjust the rates we charge for our freight brokerage, inter-modal and truckload services. The majority of our contracts for fuel purchases utilize index-based pricing formulas plus or minus a fixed locational/supplier differential. While many of the indices are aligned, each index may fluctuate at a different pace, driving variability in the prices paid for fuel. Because of this, our operating results may be affected should the market price of fuel suddenly change by a significant amount or change by amounts that do not result in an adjustment in our fuel surcharges, which can significantly affect our earnings either positively or negatively in the short-term. Additionally, we periodically use a combination of option, forward and futures contracts to provide partial protection from changing fuel and energy prices. As of December 31, 2018 and 2017, however, we had no commodity contracts outstanding.

Foreign Currency Exchange Risk

We have foreign currency risks related to our revenue, operating expenses and financing transactions in currencies other than the local currencies in which we operate. We are exposed to currency risk from the potential changes in functional currency values of our foreign currency-denominated assets, liabilities and cash flows. Our most significant foreign currency exposures relate to the Euro, British Pound Sterling, Canadian Dollar, Chinese Renminbi and Hong Kong Dollar. We use forwards as well as a combination of purchased and written options to hedge forecasted cash flow currency exposures. These derivative instruments generally cover forecasted foreign currency exposures for periods of 12 to 48 months. We also utilize forward contracts to hedge portions of our anticipated cash settlements of intercompany transactions subject to foreign currency remeasurement.

Interest Rate Risk

We have issued debt instruments, including debt associated with capital leases, that accrue expense at fixed and floating rates of interest. We use a combination of interest rate swaps as part of our program to manage the fixed and floating interest rate mix of our total debt portfolio and related overall cost of borrowing. The notional amount, interest payment and maturity dates of the swaps match the terms of the associated debt. We also utilize forward starting swaps and similar instruments to lock in all or a portion of the borrowing cost of anticipated debt issuances. Our floating-rate debt and interest rate swaps subject us to risk resulting from changes in short-term (primarily LIBOR) interest rates.

We also are subject to interest rate risk with respect to our pension and postretirement benefit obligations, as changes in interest rates will effectively increase or decrease our liabilities associated with these benefit plans, which also results in changes to the amount of pension and postretirement benefit expense recognized in future periods.

We have investments in debt securities, as well as cash-equivalent instruments, some of which accrue income at variable rates of interest. Additionally, we hold a portfolio of finance receivables that accrue income at fixed and floating rates of interest.

Sensitivity Analysis

The following analysis provides quantitative information regarding our exposure to foreign currency exchange risk, interest rate risk and equity price risk embedded in our existing financial instruments. We utilize valuation models to evaluate the sensitivity of the fair value of financial instruments with exposure to market risk that assume instantaneous, parallel shifts in exchange rates, interest rate yield curves and commodity and equity prices. For options and instruments with non-linear returns, models appropriate to the instrument are utilized to determine the impact of market shifts.

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UNITED PARCEL SERVICE, INC. AND SUBSIDIARIES  
MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND  
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There are certain limitations inherent in the sensitivity analyses presented, primarily due to the assumption that exchange rates change in a parallel fashion and that interest rates change instantaneously. In addition, the analyses are unable to reflect the complex market reactions that normally would arise from the market shifts modeled. While this is our best estimate of the impact of the specified interest rate scenarios, these estimates should not be viewed as forecasts. We adjust the fixed and floating interest rate mix of our interest rate sensitive assets and liabilities in response to changes in market conditions. Additionally, changes in the fair value of foreign currency derivatives and commodity derivatives are offset by changes in the cash flows of the underlying hedged foreign currency and commodity transactions.

(in millions)	Shock-Test Result	
	As of December 31,	
	2018	2017
Change in Fair Value:		
Currency Derivatives <sup>(1)</sup>	\$ (426 )	\$ (447 )
Change in Annual Interest Expense:		
Variable Rate Debt <sup>(2)</sup>	\$ 58	\$ 51
Interest Rate Derivatives <sup>(2)</sup>	\$ 47	\$ 55
Change in Annual Interest Income:		
Marketable Securities <sup>(3)</sup>	\$ 1	\$ 2

(1) The potential change in fair value from a hypothetical 10% weakening of the U.S. Dollar against local currency exchange rates across all maturities.

The potential change in annual interest expense resulting from a hypothetical 100 basis point increase in short-term

(2) interest rates, applied to our variable rate debt and swap instruments (excluding hedges of anticipated debt issuances).

(3) The potential change in interest income resulting from a hypothetical 100 basis point increase in short-term interest rates, applied to our variable rate investment holdings.

The sensitivity of our pension and postretirement benefit obligations to changes in interest rates is quantified in "Critical Accounting Policies and Estimates". The sensitivity in the fair value and interest income of our finance receivables due to changes in interest rates was not material as of December 31, 2018 and 2017.

Item 8. Financial Statements and Supplementary Data  
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Report of Independent Registered Public Accounting Firm  
To the Shareowners and Board of Directors of  
United Parcel Service, Inc.  
Atlanta, Georgia

#### Opinion on the Financial Statements

We have audited the accompanying consolidated balance sheets of United Parcel Service, Inc. and subsidiaries (the “Company”) as of December 31, 2018 and 2017, the related consolidated statements of income, comprehensive income, and cash flows, for each of the three years in the period ended December 31, 2018, and the related notes (collectively referred to as the “financial statements”). In our opinion, the financial statements present fairly, in all material respects, the financial position of the Company as of December 31, 2018 and 2017, and the results of its operations and its cash flows for each of the three years in the period ended December 31, 2018, in conformity with accounting principles generally accepted in the United States of America.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States) (“PCAOB”), the Company's internal control over financial reporting as of December 31, 2018, based on criteria established in Internal Control - Integrated Framework (2013) issued by the Committee of Sponsoring Organizations of the Treadway Commission and our report dated February 21, 2019, expressed an unqualified opinion on the Company's internal control over financial reporting.

#### Change in Accounting Principles

As discussed in Note 1 to the financial statements, the Company has changed its method of accounting for revenue from contracts with customers and the presentation of net periodic benefit costs due to the adoption of new accounting standards. These changes have been applied retrospectively to all periods presented.

#### Basis for Opinion

These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on the Company's financial statements based on our audits. We are a public accounting firm registered with the PCAOB and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB. We conducted our audits in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement, whether due to error or fraud. Our audits included performing procedures to assess the risks of material misstatement of the financial statements, whether due to error or fraud, and performing procedures that respond to those risks. Such procedures included examining, on a test basis, evidence regarding the amounts and disclosures in the financial statements. Our audits also included evaluating the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the financial statements. We believe that our audits provide a reasonable basis for our opinion.

/s/ Deloitte & Touche LLP  
Atlanta, Georgia  
February 21, 2019

We have served as the Company's auditor since 1969.



UNITED PARCEL SERVICE, INC. AND SUBSIDIARIES  
CONSOLIDATED BALANCE SHEETS  
(In millions)

	December 31,	
	2018	2017
<b>ASSETS</b>		
Current Assets:		
Cash and cash equivalents	\$4,225	\$3,320
Marketable securities	810	749
Accounts receivable, net	8,958	8,773
Current income taxes receivable	940	1,573
Other current assets	1,277	1,303
Total Current Assets	16,210	15,718
Property, Plant and Equipment, Net	26,576	22,118
Goodwill	3,811	3,872
Intangible Assets, Net	2,075	1,964
Investments and Restricted Cash	170	483
Deferred Income Tax Assets	141	266
Other Non-Current Assets	1,033	1,153
Total Assets	\$50,016	\$45,574
<b>LIABILITIES AND SHAREOWNERS' EQUITY</b>		
Current Liabilities:		
Current maturities of long-term debt and commercial paper	\$2,805	\$4,011
Accounts payable	5,188	3,934
Accrued wages and withholdings	3,047	2,608
Self-insurance reserves	810	705
Accrued group welfare and retirement plan contributions	715	677
Other current liabilities	1,522	951
Total Current Liabilities	14,087	12,886
Long-Term Debt	19,931	20,278
Pension and Postretirement Benefit Obligations	8,347	7,061
Deferred Income Tax Liabilities	1,619	756
Self-Insurance Reserves	1,571	1,765
Other Non-Current Liabilities	1,424	1,804
Shareowners' Equity:		
Class A common stock (163 and 173 shares issued in 2018 and 2017)	2	2
Class B common stock (696 and 687 shares issued in 2018 and 2017)	7	7
Additional paid-in capital	—	—
Retained earnings	8,006	5,852
Accumulated other comprehensive loss	(4,994 )	(4,867 )
Deferred compensation obligations	32	37
Less: Treasury stock (1 share in 2018 and 2017)	(32 )	(37 )
Total Equity for Controlling Interests	3,021	994
Noncontrolling Interests	16	30

Total Shareowners' Equity	3,037	1,024
Total Liabilities and Shareowners' Equity	\$50,016	\$45,574

See notes to consolidated financial statements.

## UNITED PARCEL SERVICE, INC. AND SUBSIDIARIES

## STATEMENTS OF CONSOLIDATED INCOME

(In millions, except per share amounts)

	Years Ended December 31,		
	2018	2017	2016
Revenue	\$71,861	\$66,585	\$61,610
Operating Expenses:			
Compensation and benefits	37,235	34,577	32,534
Repairs and maintenance	1,732	1,601	1,542
Depreciation and amortization	2,207	2,282	2,224
Purchased transportation	13,409	11,696	9,848
Fuel	3,427	2,690	2,118
Other occupancy	1,362	1,155	1,037
Other expenses	5,465	5,055	4,619
Total Operating Expenses	64,837	59,056	53,922
Operating Profit	7,024	7,529	7,688
Other Income and (Expense):			
Investment income (expense) and other	(400 )	61	(2,186 )
Interest expense	(605 )	(453 )	(381 )
Total Other Income and (Expense)	(1,005 )	(392 )	(2,567 )
Income Before Income Taxes	6,019	7,137	5,121
Income Tax Expense	1,228	2,232	1,699
Net Income	\$4,791	\$4,905	\$3,422
Basic Earnings Per Share	\$5.53	\$5.63	\$3.88
Diluted Earnings Per Share	\$5.51	\$5.61	\$3.86

## STATEMENTS OF CONSOLIDATED COMPREHENSIVE INCOME (LOSS)

(In millions)

	Years Ended December 31,		
	2018	2017	2016
Net Income	\$ 4,791	\$ 4,905	\$ 3,422
Change in foreign currency translation adjustment, net of tax	(149 )	86	(119 )
Change in unrealized gain (loss) on marketable securities, net of tax	—	(1 )	—
Change in unrealized gain (loss) on cash flow hedges, net of tax	485	(321 )	(112 )
Change in unrecognized pension and postretirement benefit costs, net of	272	(148 )	(712 )

tax

Comprehensive Income (Loss)	\$ 5,399	\$ 4,521	\$ 2,479
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See notes to consolidated financial statements.

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UNITED PARCEL SERVICE, INC. AND SUBSIDIARIES  
 STATEMENTS OF CONSOLIDATED CASH FLOWS  
 (In millions)

	Years Ended		
	December 31,		
	2018	2017	2016
<b>Cash Flows From Operating Activities:</b>			
Net income	\$4,791	\$4,905	\$3,422
Adjustments to reconcile net income to net cash from operating activities:			
Depreciation and amortization	2,207	2,282	2,224
Pension and postretirement benefit expense	2,242	1,643	3,725
Pension and postretirement benefit contributions	(186 )	(7,794 )	(2,668 )
Self-insurance reserves	(86 )	—	(21 )
Deferred tax (benefit) expense	758	1,224	117
Stock compensation expense	634	584	591
Other (gains) losses	293	37	(198 )
Changes in assets and liabilities, net of effects of business acquisitions:			
Accounts receivable	(421 )	(1,022 )	(704 )
Other assets	754	(984 )	5
Accounts payable	1,034	599	460
Accrued wages and withholdings	505	200	91
Other liabilities	170	(243 )	(546 )
Other operating activities	16	48	(25 )
Net cash from operating activities	12,711	1,479	6,473
<b>Cash Flows From Investing Activities:</b>			
Capital expenditures	(6,283 )	(5,227 )	(2,965 )
Proceeds from disposals of property, plant and equipment	37	24	88
Purchases of marketable securities	(973 )	(1,630 )	(4,813 )
Sales and maturities of marketable securities	886	1,990	5,724
Net (increase) decrease in finance receivables	4	5	9
Cash paid for business acquisitions, net of cash and cash equivalents acquired	(2 )	(134 )	(547 )
Other investing activities	1	1	(59 )
Net cash used in investing activities	(6,330 )	(4,971 )	(2,563 )
<b>Cash Flows From Financing Activities:</b>			
Net change in short-term debt	63	(250 )	(88 )
Proceeds from long-term borrowings	1,202	12,016	5,927
Repayments of long-term borrowings	(2,887 )	(3,939 )	(3,805 )
Purchases of common stock	(1,011 )	(1,813 )	(2,678 )
Issuances of common stock	240	247	245
Dividends	(3,011 )	(2,771 )	(2,643 )
Other financing activities	(288 )	(203 )	(98 )
Net cash used in financing activities	(5,692 )	3,287	(3,140 )
Effect Of Exchange Rate Changes On Cash, Cash Equivalents and Restricted Cash	(91 )	53	(21 )
Net Increase (Decrease) In Cash, Cash Equivalents and Restricted Cash	598	(152 )	749

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Cash, Cash Equivalents and Restricted Cash:

Beginning of period	3,769	3,921	3,172
End of period	\$4,367	\$3,769	\$3,921

Cash Paid During The Period For:

Interest (net of amount capitalized)	\$595	\$428	\$373
Income taxes (net of refunds and overpayments)	\$2	\$1,559	\$2,064

See notes to consolidated financial statements.

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UNITED PARCEL SERVICE, INC. AND SUBSIDIARIES  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
NOTE 1. SUMMARY OF ACCOUNTING POLICIES

Basis of Financial Statements and Business Activities

The accompanying consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States (“GAAP”), and include the accounts of United Parcel Service, Inc., and all of its consolidated subsidiaries (collectively “UPS” or the “Company”). All intercompany balances and transactions have been eliminated.

UPS concentrates its operations in the field of transportation services, primarily domestic and international letter and package delivery. Through our Supply Chain & Freight subsidiaries, we are also a global provider of specialized transportation, logistics and financial services.

Use of Estimates

The preparation of our consolidated financial statements requires the use of estimates and assumptions that affect the reported amounts of assets and liabilities, the reported amounts of revenues and expenses and the disclosure of contingencies. Estimates have been prepared on the basis of the most current and best information, and actual results could differ materially from those estimates.

Revenue Recognition

U.S. Domestic and International Package Operations—Revenue is recognized over time as we perform the services in the contract.

Forwarding —Freight forwarding revenue and the expense related to the transportation of freight are recognized over time as we perform the services. Truckload brokerage revenue and related transportation costs are recognized over time as we perform the services. Customs brokerage revenue is recognized upon completing documents necessary for customs entry purposes.

Logistics —In our Logistics business we have a right to consideration from customers in an amount that corresponds directly with the value to the customers of our performance completed to date, and as such we recognize revenue in the amount to which we have a right to invoice the customer.

UPS Freight—Revenue is recognized over time as we perform the services in the contract.

In our transportation businesses, we utilize independent contractors and third-party carriers in the performance of some transportation services. U.S. GAAP requires us to evaluate whether our businesses themselves promise to transfer services to the customer (as the principal) or to arrange for services to be provided by another party (as the agent) using a control model. Based on our evaluation of the control model, we determined that all of our major businesses act as the principal rather than the agent within their revenue arrangements. Revenue and the associated purchased transportation costs are reported on a gross basis within our statements of consolidated income.

Financial Services—Income on loans and direct finance leases is recognized on the effective interest method. Accrual of interest income is suspended at the earlier of the time at which collection of an account becomes doubtful or the account becomes 90 days delinquent. Income on operating leases is recognized on the straight-line method over the terms of the underlying leases.

Refer to note 2 of our audited consolidated financial statements for further discussion of our revenue recognition policies.

Cash and Cash Equivalents

Cash and cash equivalents consist of highly liquid investments that are readily convertible into cash. We consider securities with maturities of three months or less, when purchased, to be cash equivalents. The carrying amount of these securities approximates fair value because of the short-term maturity of these instruments.



UNITED PARCEL SERVICE, INC. AND SUBSIDIARIES  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

### Investments

Marketable securities are either classified as trading or available-for-sale securities and are carried at fair value. Unrealized gains and losses on trading securities are reported as investment income (expense) and other on the statements of consolidated income. Unrealized gains and losses on available-for-sale securities are reported as accumulated other comprehensive income (“AOCI”), a separate component of shareowners’ equity. The amortized cost of debt securities is adjusted for amortization of premiums and accretion of discounts to maturity. Such amortization and accretion is included in investment income (expense) and other, along with interest and dividends. The cost of securities sold is based on the specific identification method; realized gains and losses resulting from such sales are included in investment income (expense) and other.

We periodically review our available-for-sale investments for indications of other-than-temporary impairment considering many factors, including the extent and duration to which a security’s fair value has been less than its cost, overall economic and market conditions and the financial condition and specific prospects for the issuer. Impairment of available-for-sale securities results in a charge to income when a market decline below cost is other-than-temporary.

### Accounts Receivable

Accounts receivable, net, include amounts billed and currently due from customers. The amounts due are stated at their net estimated realizable value. Losses on accounts receivable are recognized when they are incurred, which requires us to make our best estimate of the probable losses inherent in our customer receivables at each balance sheet date. These estimates require consideration of historical loss experience, adjusted for current conditions, trends in customer payment frequency and judgments about the probable effects of relevant observable data, including present economic conditions and the financial health of specific customers and market sectors. Our risk management process includes standards and policies for reviewing major account exposures and concentrations of risk.

Our total allowance for doubtful accounts as of December 31, 2018 and 2017 was \$94 and \$104 million, respectively. Our total provision for doubtful accounts charged to expense before recoveries during the years ended December 31, 2018, 2017 and 2016 was \$118, \$133 and \$116 million, respectively.

### Inventories

Fuel and other materials and supplies inventories are recognized as inventory when purchased, and then charged to expense when used in our operations. Jet fuel, diesel and unleaded gasoline inventories are valued at the lower of average cost or market. Total inventories were \$421 and \$404 million as of December 31, 2018 and 2017, respectively, and are included in “other current assets” on the consolidated balance sheets.

### Property, Plant and Equipment

Property, plant and equipment are carried at cost. We evaluate the useful lives of our property, plant and equipment based on our usage, maintenance and replacement policies, and taking into account physical and economic factors that may affect the useful lives of the assets. As part of our ongoing investment in transformation in 2018, we revised our estimates of useful lives for building improvements, vehicles and plant equipment based on our current assessment of these factors. In general, the change in estimate had the effect of lengthening the useful lives of building improvements, vehicles and plant equipment.

Depreciation and amortization are provided by the straight-line method over the estimated useful lives of the assets, which are as follows: Vehicles—6 to 15 years; Aircraft—12 to 30 years; Buildings—20 to 40 years; Leasehold Improvements—lesser of asset useful life or lease term; Plant Equipment—3 to 20 years; Technology Equipment—3 to 5 years. For substantially all of our aircraft, the costs of major airframe and engine overhauls, as well as routine maintenance and repairs, are charged to expense as incurred.

Interest incurred during the construction period of certain property, plant and equipment is capitalized until the underlying assets are placed in service, at which time amortization of the capitalized interest begins, straight-line, over

the estimated useful lives of the related assets. Capitalized interest was \$97, \$49 and \$14 million for 2018, 2017, and 2016, respectively.

We review long-lived assets for impairment when circumstances indicate the carrying amount of an asset may not be recoverable based on the undiscounted future cash flows of the asset. If the carrying amount of the asset is determined not to be recoverable, a write-down to fair value is recorded. Fair values are determined based on quoted market values, discounted cash flows, or external appraisals, as appropriate. We review long-lived assets for impairment at the individual asset or the asset group level for which the lowest level of independent cash flows can be identified.

UNITED PARCEL SERVICE, INC. AND SUBSIDIARIES  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

### Goodwill and Intangible Assets

Costs of purchased businesses in excess of net identifiable assets acquired (goodwill), and indefinite-lived intangible assets are tested for impairment at least annually, unless changes in circumstances indicate an impairment may have occurred sooner. We are required to test goodwill on a “reporting unit” basis. A reporting unit is the operating segment unless, for businesses within that operating segment, discrete financial information is prepared and regularly reviewed by management, in which case such a component business is the reporting unit.

In assessing goodwill for impairment, we initially evaluate qualitative factors to determine if it is more likely than not that the fair value of a reporting unit is less than its carrying amount. We consider several factors, including macroeconomic conditions, industry and market conditions, overall financial performance of the reporting unit, changes in management, strategy or customers and relevant reporting unit-specific events such as a change in the carrying amount of net assets, a more likely than not expectation of selling or disposing all, or a portion, of a reporting unit, and the testing for recoverability of a significant asset group within a reporting unit. If this qualitative assessment results in a conclusion that it is more likely than not that the fair value of a reporting unit exceeds the carrying value, then no further testing is performed for that reporting unit.

If the qualitative assessment is not conclusive and it is necessary to calculate the fair value of a reporting unit, then we utilize a two-step process to test goodwill for impairment. First, a comparison of the fair value of the applicable reporting unit with the aggregate carrying value, including goodwill, is performed. If the carrying amount of a reporting unit exceeds its calculated fair value, then the second step is performed, and an impairment charge is recognized for the amount, if any, by which the carrying amount of goodwill exceeds its implied fair value. We primarily determine the fair value of our reporting units using a discounted cash flow model and supplement this with observable valuation multiples for comparable companies, as appropriate.

A trade name with a carrying value of \$200 million and licenses with a carrying value of \$5 million as of December 31, 2018 are considered to be indefinite-lived intangibles, and therefore are not amortized. Indefinite-lived intangible assets are reviewed for impairment at least annually. We determined that the income approach, specifically the relief from royalty method, is the most appropriate valuation method to estimate the fair value of the trade name. The estimated fair value of the trade name is compared to the carrying value of the asset. If the carrying value of the trade name exceeds its estimated fair value, an impairment charge is recognized for the amount by which the carrying amount of the asset exceeds its fair value.

Finite-lived intangible assets, including trademarks, licenses, patents, customer lists, non-compete agreements and franchise rights are amortized on a straight-line basis over the estimated useful lives of the assets, which range from 2 to 22 years. Capitalized software is generally amortized over 7 years.

### Self-Insurance Accruals

We self-insure costs associated with workers’ compensation claims, automobile liability, health and welfare and general business liabilities, up to certain limits. Insurance reserves are established for estimates of the loss that we will ultimately incur on reported claims, as well as estimates of claims that have been incurred but not yet reported. Recorded balances are based on reserve levels, which incorporate historical loss experience and judgments about the present and expected levels of cost per claim. Trends in actual experience are a significant factor in the determination of such reserves.

Workers’ compensation, automobile liability and general liability insurance claims may take several years to completely settle. Consequently, actuarial estimates are required to project the ultimate cost that will be incurred to fully resolve the claims. A number of factors can affect the actual cost of a claim, including the length of time the claim remains open, trends in healthcare costs and the results of related litigation. Furthermore, claims may emerge in future years for events that occurred in a prior year at a rate that differs from previous actuarial projections. Changes in state legislation with respect to workers' compensation can affect the adequacy of our self-insurance accruals. All of

these factors can result in revisions to prior actuarial projections and produce a material difference between estimated and actual operating results. Prior to 2017, outside actuarial studies were performed semi-annually and we used the studies to estimate the liability in intervening quarters. Beginning in 2017, outside actuarial studies are now performed quarterly as we believe this provides us with better quarterly estimates of our outstanding workers' compensation liability.

We sponsor a number of health and welfare insurance plans for our employees. These liabilities and related expenses are based on estimates of the number of employees and eligible dependents covered under the plans, anticipated medical usage by participants and overall trends in medical costs and inflation.



UNITED PARCEL SERVICE, INC. AND SUBSIDIARIES  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

#### Pension and Postretirement Benefits

We incur certain employment-related expenses associated with pension and postretirement medical benefits. These pension and postretirement medical benefit costs for company-sponsored benefit plans are calculated using various actuarial assumptions and methodologies, including discount rates, expected returns on plan assets, healthcare cost trend rates, inflation, compensation increase rates, mortality rates and coordination of benefits with plans not sponsored by UPS. Actuarial assumptions are reviewed on an annual basis, unless circumstances require an interim remeasurement for any of our plans.

We recognize changes in the fair value of plan assets and net actuarial gains or losses in excess of a corridor (defined as 10% of the greater of the fair value of plan assets or the plans' projected benefit obligations) in pension expense annually at December 31st each year. The remaining components of pension expense, primarily service and interest costs and the expected return on plan assets, are recorded on a quarterly basis.

Effective July 1, 2016, the UPS Retirement Plan was closed to new non-union participants. For eligible employees hired after July 1, 2016, UPS contributes annually to a defined contribution plan. We recognize expense for the required contribution quarterly, and we recognize a liability for any contributions due and unpaid (included in "other current liabilities").

During June 2017, we amended the UPS Retirement Plan and Excess Coordinating Plan to cease accrual of additional benefits for future service for non-union participants effective January 1, 2023. We remeasured plan assets and pension benefit obligations for the affected pension plans as of June 30, 2017 to recognize the impact of this change. We participate in a number of trustee-managed multiemployer pension and health and welfare plans for employees covered under collective bargaining agreements. Our contributions to these plans are determined in accordance with the respective collective bargaining agreements. We recognize expense for the contractually required contribution for each period, and we recognize a liability for any contributions due and unpaid (included in "other current liabilities").

#### Income Taxes

Income taxes are accounted for on an asset and liability approach that requires the recognition of deferred tax assets and liabilities for the expected future tax consequences of events that have been recognized in our consolidated financial statements or tax returns. In estimating future tax consequences, we generally consider all expected future events other than proposed changes in the tax law or rates. Valuation allowances are provided if it is more likely than not that a deferred tax asset will not be realized.

We recognize liabilities for uncertain tax positions based on a two-step process. The first step is to evaluate the tax position for recognition by determining if the weight of available evidence indicates that it is more likely than not that the position will be sustained on audit, including resolution of related appeals or litigation processes, if any. Once it is determined that the position meets the recognition threshold, the second step requires us to estimate and measure the largest amount of tax benefit that is more likely than not to be realized upon ultimate settlement. The difference between the amount of recognizable tax benefit and the total amount of tax benefit from positions filed or to be filed with the tax authorities is recorded as a liability for uncertain tax benefits. It is inherently difficult and subjective to estimate such amounts, as we have to determine the probability of various possible outcomes. We reevaluate uncertain tax positions on a quarterly basis. This evaluation is based on factors including, but not limited to, changes in facts or circumstances, changes in tax law, effectively settled issues under audit and new audit activity. Such a change in recognition or measurement could result in the recognition of a tax benefit or an additional charge to the tax provision. In January 2018, the Financial Accounting Standards Board ("FASB") released guidance on the accounting for tax on the Global Intangible Low-Taxed Income ("GILTI") provisions of the Tax Cuts and Jobs Act (the "Tax Act"). The GILTI provisions impose U.S. tax on certain foreign income in excess of a deemed return on tangible assets of foreign corporations. The guidance indicates that either accounting for deferred taxes related to GILTI inclusions or treating

any taxes on GILTI inclusions as period costs are both acceptable methods subject to an accounting policy election. We elect to treat any potential GILTI inclusions as period costs.

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UNITED PARCEL SERVICE, INC. AND SUBSIDIARIES  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

#### Foreign Currency Translation and Remeasurement

We translate the results of operations of our foreign subsidiaries using average exchange rates during each period, whereas balance sheet accounts are translated using exchange rates at the end of each period. Balance sheet currency translation adjustments are recorded in AOCI. Pre-tax foreign currency transaction gains (losses) from remeasurement, net of hedging, included in investment income (expense) and other were \$(19), \$3 and \$5 million in 2018, 2017 and 2016, respectively.

#### Stock-Based Compensation

All share-based awards to employees are measured based on their fair values and expensed over the period during which an employee is required to provide service in exchange for the award (the vesting period), less estimated forfeitures. We issue employee share-based awards under the UPS Incentive Compensation Plan that are subject to specific vesting conditions; including service conditions, where the awards cliff vest or vest ratably over a three or five year period (the "nominal vesting period") or at the date the employee retires (as defined by the plan), if earlier. Compensation cost is generally recognized immediately for awards granted to retirement-eligible employees, or over the period from the grant date to the date retirement eligibility is achieved, if that is expected to occur during the nominal vesting period. We estimate forfeiture rates based on historical rates of forfeitures for awards with similar characteristics, historical rates of employee turnover and the nature and terms of the vesting conditions of the awards. We reevaluate our forfeiture rates on an annual basis.

#### Fair Value Measurements

Our financial assets and liabilities measured at fair value on a recurring basis have been categorized based upon a fair value hierarchy. Level 1 inputs utilize quoted prices in active markets for identical assets or liabilities. Level 2 inputs are based on other observable market data, such as quoted prices for similar assets and liabilities, and inputs other than quoted prices that are observable, such as interest rates and yield curves. Level 3 inputs are developed from unobservable data reflecting our own assumptions, and include situations where there is little or no market activity for the asset or liability.

Certain non-financial assets and liabilities are measured at fair value on a nonrecurring basis, including property, plant, and equipment, goodwill and intangible assets. These assets are not measured at fair value on a recurring basis; however, they are subject to fair value adjustments in certain circumstances, such as when there is evidence of an impairment. A general description of the valuation methodologies used for assets and liabilities measured at fair value, including the general classification of such assets and liabilities pursuant to the valuation hierarchy, is included in each footnote with fair value measurements present.

For acquisitions, we allocate the fair value of purchase consideration to the tangible assets acquired, liabilities assumed and intangible assets acquired based on their estimated fair values. The excess of the fair value of purchase consideration over the fair values of these identifiable assets and liabilities is recorded as goodwill. Such valuations require management to make significant estimates and assumptions, especially with respect to intangible assets. Significant estimates in valuing certain intangible assets include, but are not limited to, future expected cash flows from acquired customers, acquired technology and trade names from a market participant perspective, useful lives and discount rates. Management's estimates of fair value are based upon assumptions believed to be reasonable, but which are inherently uncertain and unpredictable and, as a result, actual results may differ from estimates. During the measurement period, which is one year from the acquisition date, we may record adjustments to the assets acquired and liabilities assumed, with the corresponding offset to goodwill. Upon the conclusion of the measurement period, any subsequent adjustments are recorded to earnings.

#### Derivative Instruments

All financial derivative instruments are recorded on our consolidated balance sheets at fair value. Derivatives not designated as hedges must be adjusted to fair value through income. If a derivative is designated as a hedge, changes in its fair value that are considered to be effective, as defined, either (depending on the nature of the hedge) offset the change in fair value of the hedged assets, liabilities or firm commitments through income, or are recorded in AOCI until the hedged item is recorded in income. Any portion of a change in a hedge's fair value that is considered to be ineffective, or is excluded from the measurement of effectiveness, is recorded immediately in income.

UNITED PARCEL SERVICE, INC. AND SUBSIDIARIES  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Adoption of New Accounting Standards

In May 2014, the FASB issued an accounting standards update ("ASU") that changes the revenue recognition for companies that enter into contracts with customers to transfer goods or services ("Revenue from Contracts with Customers"). The standard is a comprehensive new revenue recognition model that requires revenue to be recognized in a manner depicting the transfer of goods or services to a customer at an amount that reflects the consideration expected to be received in exchange for those goods or services. The FASB has also issued a number of updates to this standard. Effective January 1, 2018, we adopted the requirements of this ASU using the full retrospective method. See note 2 for required disclosures pertaining to the new ASU.

In January 2016, the FASB issued an ASU which addresses certain aspects of the recognition, measurement, presentation and disclosure of financial instruments. We adopted this standard on January 1, 2018. This accounting standards update does not have a material impact on our consolidated financial position, results of operations or cash flows.

In March 2016, the FASB issued an ASU that simplifies the income tax accounting and cash flow presentation related to share-based compensation by requiring the recognition of all excess tax benefits and deficiencies directly on the income statement and classification as cash flows from operating activities on the statement of cash flows. This new guidance became effective for us in the first quarter of 2017 and we adopted the statements of consolidated cash flows and statements of consolidated income presentation on a prospective basis. The impact to income tax expense in the statements of consolidated income was a benefit of \$38 and \$71 million in 2018 and 2017, respectively. Additionally, we have elected to continue estimating forfeitures expected to occur to determine the amount of compensation cost to be recognized each period.

In August 2016, the FASB issued an ASU that addresses the classification and presentation of specific cash flow issues that resulted in diverse practices. The guidance also clarifies how the predominance principle should be applied when cash receipts and cash payments have aspects of more than one class of cash flows. The guidance was applied retrospectively. We adopted this standard on January 1, 2018. This standard did not have a material impact on our statements of consolidated cash flows.

In November 2016, the FASB issued an ASU that is intended to reduce diversity in practice by adding or clarifying guidance on classification and presentation of changes in restricted cash on the statement of cash flows ("Restricted Cash"). Effective January 1, 2018, we adopted the requirements of this ASU retrospectively. As a result of this update, restricted cash is included within cash and cash equivalents on our statements of consolidated cash flows.

In March 2017, the FASB issued an ASU to improve the presentation of net periodic pension cost and net periodic postretirement benefit cost ("Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost"). The update requires employers to report the current service cost component in the same line item as other compensation costs arising from services rendered by employees during the period. The other components of net benefit cost are required to be presented separately from service cost and outside of income from operations. Effective January 1, 2018, we adopted the requirements of this ASU retrospectively, as required. As a result of this update, the net amount of interest cost, prior service cost and expected return on plan assets is now presented as other income.

In May 2017, the FASB issued an ASU to provide clarity and reduce complexity on when to apply modification accounting to existing share-based payment awards. The guidance will be applied prospectively. We adopted this standard on January 1, 2018. This accounting standards update did not have a material impact on our consolidated financial position, results of operations or cash flows.

In February 2018, the FASB issued an ASU that allows a reclassification from accumulated other comprehensive income ("AOCI") to retained earnings for stranded tax effects resulting from the Tax Cuts and Jobs Act (the "Tax Act"). Effective January 1, 2018, we early adopted this ASU and elected to reclassify the income tax effects of the Tax Act from AOCI to retained earnings. This resulted in a \$735 million increase to retained earnings and a \$735 million

decrease to AOCI. Our current accounting policy for releasing income tax effects from other comprehensive income is based on a portfolio approach.

In August 2018, the FASB issued an ASU that modifies the disclosure requirements for employers that sponsor defined benefit pension and postretirement plans. The update eliminates the disclosures for amounts in AOCI expected to be recognized as components of net periodic cost over the next fiscal year and the effects of a one-percentage-point change in the assumed healthcare cost trend rate. The update adds disclosure requirements to include the weighted-average interest crediting rates for cash balance plans and a narrative description of the significant gains and losses related to changes in the benefit obligation for the period. We have early adopted this standard for the year ended 2018 with retrospective application. This accounting standards update did not have a material impact on our consolidated financial position, results of operations or cash flows.

UNITED PARCEL SERVICE, INC. AND SUBSIDIARIES  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

We have recast our consolidated financial statements from amounts previously reported due to the adoption of new revenue recognition, pension and restricted cash standards. Impacted consolidated balance sheet line items, which reflect the adoption of the new ASUs, are as follows (in millions):

	December 31, 2017				
	As previously reported	Adjustments (a)	Adjustments (b)	Adjustments (c)	As Recast
<b>Assets:</b>					
Other current assets	\$ 1,133	\$ 170	\$	—\$	—\$ 1,303
Total current assets	15,548	170	—	—	15,718
Deferred income tax assets	265	1	—	—	266
Total Assets	\$45,403	\$ 171	\$	—\$	—\$45,574
<b>Liabilities:</b>					
Accounts payable	\$3,872	\$ 62	\$	—\$	—\$3,934
Accrued wages and withholdings	2,521	87	—	—	2,608
Other current liabilities <sup>(1)</sup>	905	29	—	—	934
Total current liabilities	12,708	178	—	—	12,886
Deferred income tax liabilities	757	(1 )	—	—	756
<b>Shareowners' Equity:</b>					
Retained earnings	5,858	(6 )	—	—	5,852
Total Shareowners' Equity	1,030	(6 )	—	—	1,024
Total Liabilities and Shareowners' Equity	\$45,403	\$ 171	\$	—\$	—\$45,574

(1) The caption "Other current liabilities" was presented separately from "Hedge margin liabilities" of \$17 million in the Form 10-K at December 31, 2017. These captions have been collapsed in the consolidated balance sheets as of December 31, 2018 and December 31, 2017 included within this Form 10-K.

(a) Recast to reflect the adoption of Revenue from Contracts with Customers.

(b) Recast to reflect the adoption of Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost.

(c) Recast to reflect the adoption of Restricted Cash.

UNITED PARCEL SERVICE, INC. AND SUBSIDIARIES  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

The unaudited consolidated statements of operations, which reflects the adoption of the new ASUs, are as follows (in millions):

	Twelve months ended December 31, 2016				
	As Previously Reported	Adjustments (a)	Adjustments (b)	Adjustments (c)	As Recast
Revenue	\$60,906	\$ 704	\$ —	\$ —	—\$61,610
Operating Expenses:					
Compensation and benefits	34,770	—	(2,236 )	—	32,534
Repairs and maintenance	1,538	4	—	—	1,542
Depreciation and amortization	2,224	—	—	—	2,224
Purchased transportation	9,129	719	—	—	9,848
Fuel	2,118	—	—	—	2,118
Other occupancy	1,037	—	—	—	1,037
Other expenses	4,623	(4 )	—	—	4,619
Total Operating Expenses	55,439	719	(2,236 )	—	53,922
Operating Profit	5,467	(15 )	2,236	—	7,688
Other Income and (Expense):					
Investment income (expense) and other	50	—	(2,236 )	—	(2,186 )
Interest expense	(381 )	—	—	—	(381 )
Total Other Income and (Expense)	(331 )	—	(2,236 )	—	(2,567 )
Income Before Income Taxes	5,136	(15 )	—	—	5,121
Income Tax Expense (Benefit)	1,705	(6 )	—	—	1,699
Net Income	\$3,431	\$ (9 )	\$ —	\$ —	—\$3,422
Basic Earnings Per Share	\$3.89	\$ (0.01 )	\$ —	\$ —	—\$3.88
Diluted Earnings Per Share	\$3.87	\$ (0.01 )	\$ —	\$ —	—\$3.86

(a) Recast to reflect the adoption of Revenue from Contracts with Customers.

(b) Recast to reflect the adoption of Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost.

(c) Recast to reflect the adoption of Restricted Cash.



UNITED PARCEL SERVICE, INC. AND SUBSIDIARIES  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

	Twelve months ended December 31, 2017				
	As Previously Reported	Adjustments (a)	Adjustments (b)	Adjustments (c)	As Recast
Revenue	\$65,872	\$ 713	\$ —	\$ —	—\$66,585
Operating Expenses:					
Compensation and benefits	34,588	—	(11 )	—	34,577
Repairs and maintenance	1,600	1	—	—	1,601
Depreciation and amortization	2,282	—	—	—	2,282
Purchased transportation	10,989	707	—	—	11,696
Fuel	2,690	—	—	—	2,690
Other occupancy	1,155	—	—	—	1,155
Other expenses	5,039	16	—	—	5,055
Total Operating Expenses	58,343	724	(11 )	—	59,056
Operating Profit	7,529	(11 )	11	—	7,529
Other Income and (Expense):					
Investment income (expense) and other	72	—	(11 )	—	61
Interest expense	(453 )	—	—	—	(453 )
Total Other Income and (Expense)	(381 )	—	(11 )	—	(392 )
Income Before Income Taxes	7,148	(11 )	—	—	7,137
Income Tax Expense (Benefit)	2,238	(6 )	—	—	2,232
Net Income	\$4,910	\$ (5 )	\$ —	\$ —	—\$4,905
Basic Earnings Per Share	\$5.64	\$ (0.01 )	\$ —	\$ —	—\$5.63
Diluted Earnings Per Share	\$5.61	\$ —	\$ —	\$ —	—\$5.61

(a) Recast to reflect the adoption of Revenue from Contracts with Customers.

(b) Recast to reflect the adoption of Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost.

(c) Recast to reflect the adoption of Restricted Cash.

UNITED PARCEL SERVICE, INC. AND SUBSIDIARIES  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

The unaudited impacted consolidated statement of cash flows line items, which reflect the adoption of the new ASUs, are as follows (in millions):

	Twelve Months Ended December 31, 2016				As Recast
	As Previously Reported	Adjustments (a)	Adjustments (b)	Adjustments (c)	
Net Income	\$3,431	\$ (9 )	\$ —	\$ —	\$3,422
Adjustments to reconcile net income to net cash from operating activities:					
Deferred tax (benefit) expense	123	(6 )	—	—	117
Other assets	(14 )	19	—	—	5
Accounts payable	461	(1 )	—	—	460
Accrued wages and withholdings	109	(18 )	—	—	91
Other liabilities	(561 )	15	—	—	(546 )
Cash flows from operating activities	6,473	—	—	—	6,473
Purchase of marketable securities	(4,816 )	—	—	3	(4,813 )
Net cash used in investing activities	(2,566 )	—	—	3	(2,563 )
Net decrease in cash, cash equivalents and restricted cash	746	—	—	3	749
Cash, cash equivalents and restricted cash at the beginning of period	2,730	—	—	442	3,172
Cash, cash equivalents and restricted cash at the end of period	\$3,476	\$ —	\$ —	\$ 445	\$3,921

(a) Recast to reflect the adoption of Revenue from Contracts with Customers.

(b) Recast to reflect the adoption of Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost.

(c) Recast to reflect the adoption of Restricted Cash.

UNITED PARCEL SERVICE, INC. AND SUBSIDIARIES  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

	Twelve Months Ended December 31, 2017				As Recast
	As Previously Reported	Adjustments (a)	Adjustments (b)	Adjustments (c)	
Net Income	\$4,910	\$ (5 )	\$ —	\$ —	\$4,905
Adjustments to reconcile net income to net cash from operating activities:					
Deferred tax (benefit) expense	1,230	(6 )	—	—	1,224
Other assets	(982 )	(2 )	—	—	(984 )
Accounts payable	592	7	—	—	599
Accrued wages and withholdings	193	7	—	—	200
Other liabilities	(241 )	(2 )	—	—	(243 )
Other operating activities	47	1	—	—	48
Cash flows from operating activities	1,479	—	—	—	1,479
Purchase of marketable securities	(1,634 )	—	—	4	(1,630 )
Net cash used in investing activities	(4,975 )	—	—	4	(4,971 )
Net decrease in cash, cash equivalents and restricted cash	(156 )	—	—	4	(152 )
Cash, cash equivalents and restricted cash at the beginning of period	3,476	—	—	445	3,921
Cash, cash equivalents and restricted cash at the end of period	\$3,320	\$ —	\$ —	\$ 449	\$3,769

(a) Recast to reflect the adoption of Revenue from Contracts with Customers.

(b) Recast to reflect the adoption of Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost.

(c) Recast to reflect the adoption of Restricted Cash.

#### Accounting Standards Issued But Not Yet Effective

In August 2017, the FASB issued an accounting standards update to enhance recognition of the economic results of hedging activities in the financial statements. In addition, this update makes certain targeted improvements to simplify the application of the hedge accounting guidance and increase transparency regarding the scope and results of hedging activities. The guidance will generally be applied prospectively and becomes effective for us in the first quarter of 2019, but early adoption is permitted. We are currently evaluating this update to determine the full impact of its adoption but do not expect this accounting standards update to have a material impact on our consolidated financial position, results of operations or cash flows.

In March 2017, the FASB issued an accounting standards update to require the premium on callable debt securities to be amortized to the earliest call date. The amortization period for callable debt securities purchased at a discount would not be impacted by the proposed update. Under current GAAP, premiums on callable debt securities are generally amortized over the contractual life of the security. Only in cases when an entity has a large number of similar securities is it allowed to consider estimates of principal prepayments. Amortization of the premium over the contractual life of the instrument can result in losses being recorded for the unamortized premium if the issuer exercises the call feature prior to maturity. The standard will be effective for us in the first quarter of 2019, but early adoption is permitted. We are currently evaluating this update to determine the full impact of its adoption but do not expect this accounting standards update to have a material impact on our consolidated financial position, results of operations or cash flows.

In January 2017, the FASB issued an accounting standards update to simplify the accounting for goodwill impairment. The update removes Step 2 of the goodwill impairment test, which requires a hypothetical purchase price allocation. A

goodwill impairment will now be the amount by which a reporting unit's carrying value exceeds its fair value, not to exceed the carrying amount of goodwill. The standard will be effective for us in the first quarter of 2020, but early adoption is permitted. We are currently evaluating this update to determine the full impact of its adoption but do not expect this accounting standards update to have a material impact on our consolidated financial position, results of operations or cash flows.

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In February 2016, the FASB issued ASU 2016-02, Leases (Topic 842), which requires lessees to recognize a right-of-use asset and lease liability on their balance sheet for all leases with terms beyond twelve months. The new standard also requires enhanced disclosures that will provided more transparency and information to financial statement users about our lease portfolio. Although the distinction between operating and finance leases will continue to exist under the new standard, the recognition and measurement of expenses and cash flows will not change significantly from current treatment. For finance leases, lessees will continue to recognize interest expense on the lease liability using the effective yield method, while the right-of-use asset will be amortized on a straight-line basis. For operating leases, expense will be recognized on a straight-line basis, consistent with the previous standard.

We will adopt this ASU on January 1, 2019 using the modified retrospective approach and will not restate comparative periods. We are substantially complete with our implementation plan. We plan to elect the transition package of three practical expedients permitted within the standard. In accordance with the package of practical expedients, we will not reassess initial direct costs, lease classification, or whether our contracts contain or are leases. We also made an accounting policy election to not recognize right-of-use assets and liabilities for leases with a term of 12 months or less, unless the leases include options to renew or purchase the underlying asset that are reasonably certain to be exercised.

Based on our lease portfolio as of December 31, 2018, we plan to recognize an operating lease liability and related right-of-use asset on our balance sheet of approximately \$2.6 billion, which represents the present value of our future minimum lease payments related to operating leases, primarily related to leases of real estate and aircraft. We do not anticipate material changes to our income statement or our statement of cash flows.

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## NOTE 2. REVENUE RECOGNITION

## Revenue Recognition

Substantially all of our revenues are from contracts associated with the pick-up, transportation and delivery of packages and freight (referred to hereafter as “transportation services”), whether carried out by or arranged by UPS, both domestically and internationally, which generally occurs over a short period of time. Additionally, we provide value-added logistics services to customers through our global network of company-owned and leased distribution centers and field stocking locations, both domestically and internationally.

## Disaggregation of Revenue

	Year Ended December 31,		
	2018	2017	2016
Revenue:			
Next Day Air	\$7,618	\$7,088	\$6,752
Deferred	4,752	4,422	4,080
Ground	31,223	29,251	27,452
U.S. Domestic Package	\$43,593	\$40,761	\$38,284
Domestic	\$2,874	\$2,646	\$2,441
Export	10,973	10,170	9,369
Cargo & Other	595	526	536
International Package	\$14,442	\$13,342	\$12,346
Forwarding	\$6,580	\$5,674	\$4,873
Logistics	3,234	3,017	2,644
Freight	3,218	3,000	2,737
Other	794	791	726
Supply Chain & Freight	\$13,826	\$12,482	\$10,980
Consolidated revenue	\$71,861	\$66,585	\$61,610

We account for a contract when both parties have approved the contract and are committed to perform their obligations, the rights of the parties are identified, payment terms are identified, the contract has commercial substance and collectability of consideration is probable. See note 1 for the adoption of new accounting standards.

## Performance Obligations

A performance obligation is a promise in a contract to transfer a distinct good or service to the customer, and is the basis of revenue recognition in accordance with U.S. GAAP. To determine the proper revenue recognition method for contracts, we evaluate whether two or more contracts should be combined and accounted for as one single contract and whether the combined or single contract should be accounted for as more than one performance obligation. This evaluation requires judgment, and the decision to combine a group of contracts or separate the combined or single contract into multiple performance obligations could change the amount of revenue and profit recorded in a given period. For most of our contracts, the customer contracts with us to provide distinct services within a contract, such as transportation services. The vast majority of our contracts with customers for transportation services include only one performance obligation, the transportation services themselves. However, if a contract is separated into more than one performance obligation, we allocate the total transaction price to each performance obligation in an amount based on the estimated relative standalone selling prices of the promised goods or services underlying each performance

obligation. We frequently sell standard transportation services with observable standalone sales prices. In these instances, the observable standalone sales are used to determine the standalone selling price.

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In certain business units, such as Logistics, we sell customized, customer-specific solutions in which we provide a significant service of integrating a complex set of tasks and components into a single capability (even if that single capability results in the delivery of multiple units). Hence, the entire contract is accounted for as one performance obligation. In these cases we typically use the expected cost plus a margin approach to estimate the standalone selling price of each performance obligation.

**Satisfaction of Performance Obligations**

We generally recognize revenue over time as we perform the services in the contract because of the continuous transfer of control to the customer. Our customers receive the benefit of our services as the goods are transported from one location to another. Further, if we were unable to complete delivery to the final location, another entity would not need to reperform the transportation service already performed.

As control transfers over time, revenue is recognized based on the extent of progress towards completion of the performance obligation. The selection of the method to measure progress towards completion requires judgment and is based on the nature of the products or services to be provided. We use the cost-to-cost measure of progress for our package delivery contracts because it best depicts the transfer of control to the customer which occurs as we incur costs on our contracts. Under the cost-to-cost measure of progress, the extent of progress towards completion is measured based on the ratio of costs incurred to date to the total estimated costs at completion of the performance obligation. Revenues, including ancillary or accessorial fees and reductions for estimated customer incentives, are recorded proportionally as costs are incurred. Costs to fulfill include labor and other direct costs and an allocation of indirect costs. For our freight and freight forwarding contracts, an output method of progress based on time-in-transit is utilized as the timing of costs incurred does not best depict the transfer of control to the customer. In our Logistics business we have a right to consideration from customers in an amount that corresponds directly with the value to the customers of our performance completed to date, and as such we recognize revenue in the amount to which we have a right to invoice the customer.

**Variable Consideration**

It is common for our contracts to contain customer incentives, guaranteed service refunds or other provisions that can either increase or decrease the transaction price. These variable amounts are generally awarded upon achievement of certain incentive tiers or performance metrics. We estimate variable consideration at the most likely amount to which we expect to be entitled. We include estimated amounts of revenue, which may be reduced by incentives or other contract provisions, in the transaction price to the extent it is probable that a significant reversal of cumulative revenue recognized will not occur when the uncertainty associated with the variable consideration is resolved. Our estimates of variable consideration and determination of whether to include estimated amounts in the transaction price are based on an assessment of anticipated customer spending and all information (historical, current and forecasted) that is reasonably available to us.

**Contract Modifications**

Contracts are often modified to account for changes in the rates we charge our customers or to add additional distinct services. We consider contract modifications to exist when the modification either creates new or changes the existing enforceable rights and obligations. Contract modifications that add additional distinct goods or services are treated as separate contracts. Contract modifications that do not add distinct goods or services typically change the price of existing services. These contract modifications will be accounted for prospectively as the remaining performance obligations are distinct.

**Payment Terms**

Under the typical payment terms of our customer contracts, the customer pays at periodic intervals (i.e., every 14 days, 30 days, 45 days, etc.) for shipments included on invoices received. Invoices are generated each week on the week-ending day, which is Saturday for the majority of our U.S. Domestic Package business, but could be another day



depending on the business unit or the specific agreement with the customer. It is not customary business practice to extend payment terms past 90 days, and as such, we do not have a practice of including a significant financing component within our revenue contracts with customers.

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Principal vs. Agent Considerations

In our transportation businesses, we utilize independent contractors and third-party carriers in the performance of some transportation services. U.S. GAAP requires us to evaluate whether our businesses themselves promise to transfer services to the customer (as the principal) or to arrange for services to be provided by another party (as the agent) using a control model. Based on our evaluation of the control model, we determined that all of our major businesses act as the principal rather than the agent within their revenue arrangements. This required a change in reporting for certain of our Supply Chain & Freight businesses where previously revenue was reported net of associated purchased transportation costs. Revenue and the associated purchased transportation costs are now both reported on a gross basis within our statements of consolidated income.

Contract Assets and Liabilities

Contract assets include billed and unbilled amounts resulting from in-transit packages, as we have an unconditional right to payment only once all performance obligations have been completed (i.e., packages have been delivered), and our right to payment is not solely based on the passage of time. Amounts may not exceed their net realizable value. Contract assets are generally classified as current and the full balance is converted each quarter based on the short-term nature of the transactions.

Contract liabilities consist of advance payments and billings in excess of revenue as well as deferred revenue. Advance payments and billings in excess of revenue represent payments received from our customers that will be earned over the contract term. Deferred revenue represents the amount of consideration due from customers related to in-transit shipments that has not yet been recognized as revenue based on our selected measure of progress. We classify advance payments and billings in excess of revenue as either current or long-term, depending on the period over which the advance payment will be earned. We classify deferred revenue as current based on the timing of when we expect to recognize revenue, which typically occurs within a short window after period-end. The full balance of deferred revenue is converted each quarter based on the short-term nature of the transactions. Our contract assets and liabilities are reported in a net position on a contract-by-contract basis at the end of each reporting period. In order to determine revenue recognized in the period from contract liabilities, we first allocate revenue to the individual contract liability balance outstanding at the beginning of the period until the revenue exceeds that deferred revenue balance.

Contract assets related to in-transit packages were \$234 and \$170 million at December 31, 2018 and 2017, respectively, net of deferred revenue related to in-transit packages of \$236 and \$174 million at December 31, 2018 and 2017, respectively. Contract assets are included within "Other current assets" in the consolidated balance sheets. Short-term contract liabilities related to advanced payments from customers were \$5 and \$31 million at December 31, 2018 and 2017, respectively. Short-term contract liabilities are included within "Other current liabilities" in the consolidated balance sheets. Long-term contract liabilities related to advanced payments from customers were \$26 million at December 31, 2018 and \$0 at December 31, 2017, respectively. Long-term contract liabilities are included within "Other Non-Current liabilities" in the consolidated balance sheets.

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## NOTE 3. INVESTMENTS AND RESTRICTED CASH

The following is a summary of marketable securities classified as trading and available-for-sale at December 31, 2018 and 2017 (in millions):

	Cost	Unrealized Gains	Unrealized Losses	Estimated Fair Value
2018				
Current trading marketable securities:				
Corporate debt securities	\$137	\$ —	\$ —	\$ 137
Equity securities	2	—	—	2
Total trading marketable securities	139	—	—	139
Current available-for-sale marketable securities:				
U.S. government and agency debt securities	297	1	(1 )	297
Mortgage and asset-backed debt securities	82	—	(1 )	81
Corporate debt securities	275	—	(2 )	273
Non-U.S. government debt securities	20	—	—	20
Total available-for-sale marketable securities	674	1	(4 )	671
Total current marketable securities	\$813	\$ 1	\$ (4 )	\$ 810
2017				
Current trading marketable securities:				
Corporate debt securities	\$75	\$ —	\$ —	\$ 75
Carbon credit investments <sup>(1)</sup>	77	16	—	93
Total trading marketable securities	152	16	—	168
Current available-for-sale marketable securities:				
U.S. government and agency debt securities	286	—	(3 )	283
Mortgage and asset-backed debt securities	86	—	—	86
Corporate debt securities	201	1	(1 )	201
Equity securities	2	—	—	2
Non-U.S. government debt securities	9	—	—	9
Total available-for-sale marketable securities	584	1	(4 )	581
Total current marketable securities	\$736	\$ 17	\$ (4 )	\$ 749

<sup>(1)</sup> These investments are hedged with forward contracts that are not designated in hedging relationships. See note 15 for offsetting statement of consolidated income impact. Total current marketable securities that were pledged as collateral for our self-insurance requirements had an estimated fair value of \$587 and \$579 million at December 31, 2018 and 2017, respectively.

There were no gross realized gains on sales of available-for-sale securities in 2018 or 2017. Gross realized gains on sales of available-for-sale securities totaled \$1 million in 2016. The gross realized losses on sales of available-for-sale securities totaled \$4, \$2 and \$1 million in 2018, 2017, and 2016, respectively.

There were no material impairment losses recognized on marketable securities during 2018, 2017 or 2016.

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#### Investment Other-Than-Temporary Impairments

We have concluded that no material other-than-temporary impairment losses existed as of December 31, 2018. In making this determination, we considered the financial condition and prospects of the issuer, the magnitude of the losses compared with the investments' cost, the probability that we will be unable to collect all amounts due according to the contractual terms of the security, the credit rating of the security and our ability and intent to hold these investments until the anticipated recovery in market value occurs.

#### Unrealized Losses

The following table presents the age of gross unrealized losses and fair value by investment category for all securities in a loss position as of December 31, 2018 (in millions):

	Less Than 12 Months		12 Months or More		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
U.S. government and agency debt securities	\$54	\$	—\$111	\$ (2 )	\$165	\$ (2 )
Mortgage and asset-backed debt securities	24	—	36	(1 )	60	(1 )
Corporate debt securities	99	—	81	(2 )	180	(2 )
Non-U.S. government debt securities	—	—	5	—	5	—
Total marketable securities	\$177	\$	—\$233	\$ (5 )	\$410	\$ (5 )

The unrealized losses for the corporate debt securities, mortgage and asset-backed debt securities and U.S. government and agency debt securities are primarily due to changes in market interest rates. We have both the intent and ability to hold the securities contained in the previous table for a time necessary to recover the cost basis.

#### Maturity Information

The amortized cost and estimated fair value of marketable securities at December 31, 2018, by contractual maturity, are shown below (in millions). Actual maturities may differ from contractual maturities because the issuers of the securities may have the right to prepay obligations without prepayment penalties.

	Cost	Estimated Fair Value
Due in one year or less	\$268	\$ 267
Due after one year through three years	448	447
Due after three years through five years	22	22
Due after five years	73	72
	811	808
Equity securities	2	2
	\$813	\$ 810

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#### Non-Current Investments and Restricted Cash

Investments and Restricted Cash are primarily associated with our self-insurance requirements. We entered into an escrow agreement with an insurance carrier to guarantee our self-insurance obligations. This agreement requires us to provide collateral to the insurance carrier, which is invested in money market funds and corporate and municipal bonds. Collateral provided is reflected in "Cash, Cash Equivalents and Restricted Cash" in the statements of consolidated cash flows. At December 31, 2018 and 2017, we had \$142 and \$449 million in self-insurance investments and restricted cash, respectively.

We held a \$19 million investment in a variable life insurance policy to fund benefits for the UPS Excess Coordinating Benefit Plan at December 31, 2018 and 2017, respectively. The quarterly change in investment fair value is recognized in "Investment income (expense) and other" on the statements of consolidated income. Additionally, we held escrowed cash related to the acquisition and disposition of certain assets, primarily real estate, of \$9 and \$15 million at December 31, 2018 and 2017, respectively.

The amounts described above are classified as "Non-current Investments and Restricted Cash" in the consolidated balance sheets.

A reconciliation of cash and cash equivalents and restricted cash from the consolidated balance sheets to the statements of consolidated cash flows is shown below (in millions):

	December 31, 2018	December 31, 2017	December 31, 2016
Cash and cash equivalents	\$ 4,225	\$ 3,320	\$ 3,476
Restricted cash	\$ 142	\$ 449	\$ 445
Total cash, cash equivalents and restricted cash	\$ 4,367	\$ 3,769	\$ 3,921

#### Fair Value Measurements

Marketable securities utilizing Level 1 inputs include active exchange-traded equity securities and equity index funds, and most U.S. Government debt securities, as these securities all have quoted prices in active markets. Marketable securities utilizing Level 2 inputs include asset-backed securities, corporate bonds and municipal bonds. These securities are valued using market corroborated pricing, matrix pricing or other models that utilize observable inputs such as yield curves.

We maintain holdings in certain investment partnerships that are measured at fair value utilizing Level 3 inputs (classified as "other non-current investments" in the tables below, and as "other non-current assets" in the consolidated balance sheets). These partnership holdings do not have quoted prices, nor can they be valued using inputs based on observable market data. These investments are valued internally using a discounted cash flow model with two significant inputs: (1) the after-tax cash flow projections for each partnership, and (2) a risk-adjusted discount rate consistent with the duration of the expected cash flows for each partnership. The weighted-average discount rates used to value these investments were 8.16% and 7.56% as of December 31, 2018 and 2017, respectively. These inputs and the resulting fair values are updated on a quarterly basis.

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The following table presents information about our investments measured at fair value on a recurring basis as of December 31, 2018 and 2017, and indicates the fair value hierarchy of the valuation techniques utilized to determine such fair value (in millions):

	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total
2018				
Marketable securities:				
U.S. government and agency debt securities	\$ 297	\$ —	\$ —	\$ 297
Mortgage and asset-backed debt securities	—	81	—	81
Corporate debt securities	—	410	—	410
Equity securities	—	2	—	2
Non-U.S. government debt securities	—	20	—	20
Total marketable securities	297	513	—	810
Other non-current investments	19	—	2	21
Total	\$ 316	\$ 513	\$ 2	\$ 831

	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total
2017				
Marketable securities:				
U.S. government and agency debt securities	\$ 283	\$ —	\$ —	\$ 283
Mortgage and asset-backed debt securities	—	86	—	86
Corporate debt securities	—	276	—	276
Equity securities	—	2	—	2
Non-U.S. government debt securities	—	9	—	9
Carbon credit investments	93	—	—	93
Total marketable securities	376	373	—	749
Other non-current investments	19	—	6	25
Total	\$ 395	\$ 373	\$ 6	\$ 774

There were no transfers of investments between Level 1 and Level 2 during the years ended December 31, 2018 and 2017.





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NOTE 4. PROPERTY, PLANT AND EQUIPMENT

Property, plant and equipment, including both owned assets as well as assets subject to capital leases, consists of the following as of December 31, 2018 and 2017 (in millions):

	2018	2017
Vehicles	\$9,820	\$9,365
Aircraft	17,499	16,248
Land	2,000	1,582
Buildings	4,808	4,035
Building and leasehold improvements	4,323	3,934
Plant equipment	11,833	9,387
Technology equipment	2,093	1,907
Equipment under operating leases	—	29
Construction-in-progress	2,112	2,239
	54,488	48,726
Less: Accumulated depreciation and amortization (27,912 )	(26,608 )	
	\$26,576	\$22,118

As part of our ongoing investment in transformation, in 2018 we made prospective revisions to our estimates of useful lives for building improvements, vehicles and plant equipment which in general had the effect of lengthening the useful lives of these categories. This resulted in a decrease in depreciation expense and an increase in operating income of \$286 million and an increase to net income of \$228 million or \$0.26 per share on a basic and diluted basis. Separately, capital investments in additional property, plant and equipment, net of disposals and fully-depreciated assets, resulted in an increase in depreciation expense of \$257 million and a decrease to net income of \$205 million or \$0.24 per share on a basic and diluted basis in 2018. Combining both impacts resulted in a net decrease of \$29 million to depreciation expense, and an increase to net income of \$23 million or \$0.03 per share on both a basic and diluted basis in 2018.

We continually monitor our aircraft fleet utilization in light of current and projected volume levels, aircraft fuel prices and other factors. Additionally, we monitor our other property, plant and equipment categories for any indicators that the carrying value of the assets may not be recoverable. No impairment charges on property, plant and equipment were recorded in 2018, 2017 or 2016.

NOTE 5. COMPANY - SPONSORED EMPLOYEE BENEFIT PLANS

We sponsor various retirement and pension plans, including defined benefit and defined contribution plans which cover our employees worldwide.

U.S. Pension Benefits

In the U.S. we maintain the following single-employer defined benefit pension plans: the UPS Retirement Plan, the UPS Pension Plan, the UPS/IBT Full-Time Employee Pension Plan and the UPS Excess Coordinating Benefit Plan, a non-qualified plan.

The UPS Retirement Plan is noncontributory and includes substantially all eligible employees of participating domestic subsidiaries who are not members of a collective bargaining unit, as well as certain employees covered by a collective bargaining agreement. This plan generally provides for retirement benefits based on average compensation levels earned by employees prior to retirement. Benefits payable under this plan are subject to maximum compensation limits and the annual benefit limits for a tax-qualified defined benefit plan as prescribed by the Internal Revenue Service ("IRS").

The UPS Pension Plan is noncontributory and includes certain eligible employees of participating domestic subsidiaries and members of collective bargaining units that elect to participate in the plan. This plan generally provides for retirement benefits based on service credits earned by employees prior to retirement.

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The UPS/IBT Full-Time Employee Pension Plan is noncontributory and includes employees that were previously members of the Central States Pension Fund, a multiemployer pension plan, in addition to other eligible employees who are covered under certain collective bargaining agreements. This plan generally provides for retirement benefits based on service credits earned by employees prior to retirement.

The UPS Excess Coordinating Benefit Plan is a non-qualified plan that provides benefits to certain participants in the UPS Retirement Plan for amounts that exceed the benefit limits described above.

In the year ended December 31, 2017, we amended the UPS Retirement Plan and the UPS Excess Coordinating Benefit Plan to cease accruals of additional benefits for future service and compensation for non-union participants effective January 1, 2023. We remeasured plan assets and pension benefit obligations for the affected pension plans as of June 30, 2017, resulting in a net actuarial gain of \$569 million. This reflected a curtailment gain of \$1.525 billion resulting from the benefit plan changes that was partially offset by net actuarial losses of \$956 million, driven by a reduction of approximately 32 basis points in the discount rate compared to December 31, 2016, offset by actual asset returns approximately 275 basis points above our expected return as of the remeasurement date. The net curtailment gain reduced the actuarial loss recorded in "Accumulated other comprehensive loss" in the equity section of the consolidated balance sheet. As actuarial losses were within the corridor (defined as 10% of the greater of the fair value of plan assets and the plan's projected benefit obligation), there was no impact to the statement of consolidated income as a result of this remeasurement.

The UPS Retirement Plan was closed to new non-union participants effective July 1, 2016. The Company amended the UPS 401(k) Savings Plan so that employees who previously would have been eligible for participation in the UPS Retirement Plan receive, in addition to current benefits under the UPS 401(k) Savings Plan, a UPS Retirement Contribution. For employees eligible to receive the Retirement Contribution, UPS will contribute 3% to 8% of eligible pay to the UPS 401(k) Savings Plan based on years of vesting service and business unit. Contributions will be made annually in cash to the accounts of participants.

During the fourth quarter of 2016, certain former U.S. employees were offered the option to receive a one-time payment of their vested pension benefit. Approximately 22,000 participants accepted this option, accelerating \$685 million in benefit payments during 2016 while reducing the number of participants who are due future payments from U.S. pension plans. As the cost of these settlements did not exceed the plans' service cost and interest cost for the year, the impact of the settlement was not recognized in earnings.

#### International Pension Benefits

We also sponsor various defined benefit plans covering certain of our international employees. The majority of our international obligations are for defined benefit plans in Canada and the United Kingdom. In addition, many of our international employees are covered by government-sponsored retirement and pension plans. We are not directly responsible for providing benefits to participants of government-sponsored plans.

#### U.S. Postretirement Medical Benefits

We also sponsor postretirement medical plans in the U.S. that provide healthcare benefits to our retirees who meet certain eligibility requirements and who are not otherwise covered by multiemployer plans. Generally, this includes employees with at least 10 years of service who have reached age 55 and employees who are eligible for postretirement medical benefits from a Company-sponsored plan pursuant to collective bargaining agreements. We have the right to modify or terminate certain of these plans. These benefits have been provided to certain retirees on a noncontributory basis; however, in many cases, retirees are required to contribute all or a portion of the total cost of the coverage.

#### Defined Contribution Plans

We also sponsor several defined contribution plans for all employees not covered under collective bargaining agreements, and for certain employees covered under collective bargaining agreements. The Company matches, in

shares of UPS common stock or cash, a portion of the participating employees' contributions. Matching contributions charged to expense were \$127, \$119 and \$111 million for 2018, 2017 and 2016, respectively.

Effective June 23, 2017, the Company amended the UPS 401(k) Savings Plan so that non-union employees who currently participate in the UPS Retirement Plan will, in addition to current benefits under the UPS 401(k) Savings Plan, earn a UPS Retirement Contribution beginning January 1, 2023. UPS will contribute 5% to 8% of eligible compensation to the UPS 401(k) Savings Plan based on years of vesting service. The amendment also provides for transition contributions for certain participants. There was no impact to the statement of consolidated income for 2018 and 2017 as a result of this change.

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As noted above, effective July 1, 2016, the UPS 401(k) Savings Plan was amended so that newly hired employees who previously would have been eligible for participation in the UPS Retirement Plan began receiving a UPS Retirement Contribution. Contributions associated with this amendment charged to expense were \$28, \$23 and \$4 million for 2018, 2017 and 2016 respectively.

Contributions are also made to defined contribution money purchase plans under certain collective bargaining agreements. Amounts charged to expense were \$92, \$91 and \$82 million for 2018, 2017 and 2016, respectively.

#### Net Periodic Benefit Cost

Information about net periodic benefit cost for the company-sponsored pension and postretirement defined benefit plans is as follows (in millions):

	U.S. Pension Benefits			U.S. Postretirement Medical Benefits			International Pension Benefits		
	2018	2017	2016	2018	2017	2016	2018	2017	2016
Net Periodic Benefit Cost:									
Service cost	\$1,661	\$1,543	\$1,412	\$29	\$29	\$28	\$62	\$60	\$49
Interest cost	1,799	1,813	1,828	104	112	124	45	40	41
Expected return on assets	(3,201)	(2,883)	(2,516)	(8)	(7)	(6)	(77)	(66)	(58)
Amortization of prior service cost	193	192	166	7	7	5	1	1	1
Actuarial (gain) loss	1,603	729	2,520	—	53	17	24	18	114
Curtailment and settlement loss	—	—	—	—	—	—	—	2	—
Net periodic benefit cost	\$2,055	\$1,394	\$3,410	\$132	\$194	\$168	\$55	\$55	\$147

#### Actuarial Assumptions

The table below provides the weighted-average actuarial assumptions used to determine the net periodic benefit cost.

	U.S. Pension Benefits			U.S. Postretirement Medical Benefits			International Pension Benefits		
	2018	2017	2016	2018	2017	2016	2018	2017	2016
Discount rate	3.84%	4.41%	4.86%	3.82%	4.23%	4.79%	2.78%	2.75%	3.51%
Rate of compensation increase	4.25%	4.27%	4.29%	N/A	N/A	N/A	3.22%	3.17%	3.04%
Expected return on assets	7.75%	8.75%	8.75%	7.20%	8.75%	8.75%	5.76%	5.65%	5.73%
Cash balance interest credit rate	2.50%	2.91%	3.36%	N/A	N/A	N/A	3.07%	2.65%	3.00%

The table below provides the weighted-average actuarial assumptions used to determine the benefit obligations of our plans.

	U.S. Pension Benefits		U.S. Postretirement Medical Benefits		International Pension Benefits	
	2018	2017	2018	2017	2018	2017
Discount rate	4.50 %	3.84 %	4.51 %	3.82 %	2.94 %	2.78 %
Rate of compensation increase	4.25 %	4.25 %	N/A	N/A	3.24 %	3.23 %
Cash balance interest credit rate	2.98 %	2.50 %	N/A	N/A	3.17 %	3.07 %

A discount rate is used to determine the present value of our future benefit obligations. To determine the discount rate for our U.S. pension and postretirement benefit plans, we use a bond matching approach to select specific bonds that would satisfy our projected benefit payments. We believe the bond matching approach reflects the process we would employ to settle our pension and postretirement benefit obligations. For our international plans, the discount rate is determined by matching the expected cash flows of a sample plan of similar duration to a yield curve based on

long-term, high quality fixed income debt instruments available as of the measurement date. These assumptions are updated each measurement date, which is typically annually.

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As of December 31, 2018, the impact of each basis point change in the discount rate on the projected benefit obligation of the pension and postretirement medical benefit plans is as follows (in millions):

	Increase (Decrease) in the Projected Benefit Obligation	
	Pension Benefits	Postretirement Medical Benefits
One basis point increase in discount rate	\$(69)	\$ (2 )
One basis point decrease in discount rate	73	2

The Society of Actuaries ("SOA") published mortality tables and improvement scales are used in developing the best estimate of mortality for U.S. plans. In October 2018, the SOA published an updated improvement scale which reduced expected mortality improvements from previously published scales. Based on our perspective of future longevity, we updated the mortality assumptions to incorporate this updated scale for purposes of measuring pension and other postretirement benefit obligations.

Assumptions for the expected return on plan assets are used to determine a component of net periodic benefit cost for the year. The assumption for our U.S. plans is developed using a long-term projection of returns for each asset class. Our asset allocation targets are reviewed and, if necessary, updated taking into consideration plan changes, funded status and actual performance. The expected return for each asset class is a function of passive, long-term capital market assumptions and excess returns generated from active management. The capital market assumptions used are provided by independent investment advisors, while excess return assumptions are supported by historical performance, fund mandates and investment expectations.

For plans outside the U.S., consideration is given to local market expectations of long-term returns. Strategic asset allocations are determined by plan based on the nature of liabilities and considering the demographic composition of the plan participants.

#### Actuarial Assumptions - Central States Pension Fund

UPS was a contributing employer to the Central States Pension Fund ("CSPF") until 2007 when we withdrew from the CSPF and fully funded our allocable share of unfunded vested benefits by paying a \$6.1 billion withdrawal liability. Under a collective bargaining agreement with the International Brotherhood of Teamsters ("IBT"), UPS agreed to provide coordinating benefits in the UPS/IBT Full Time Employee Pension Plan ("UPS/IBT Plan") for UPS participants whose last employer was UPS and who had not retired as of January 1, 2008 ("the UPS Transfer Group") in the event that benefits are lawfully reduced by the CSPF in the future consistent with the terms of our withdrawal agreement with the CSPF. Under our withdrawal agreement with the CSPF, benefits to the UPS Transfer Group cannot be reduced without our consent and can only be reduced in accordance with applicable law.

In December 2014, Congress passed the Multiemployer Pension Reform Act ("MPRA"). This change in law for the first time permitted multiemployer pension plans to reduce benefit payments to retirees, subject to specific guidelines in the statute and government approval. In September 2015, the CSPF submitted a proposed pension benefit reduction plan to the U.S. Department of the Treasury ("Treasury"). In May 2016, Treasury rejected the proposed plan submitted by the CSPF. In the first quarter of 2018, Congress established a Joint Select Committee to develop a recommendation to improve the solvency of multiemployer plans and the Pension Benefit Guaranty Corporation ("PBGC") before a November 30, 2018 deadline. While the Committee's efforts failed to meet its deadline, the Committee made significant progress towards finding solutions that will address the long term solvency of multiemployer pension plans. UPS will continue to work with all stakeholders, including legislators and regulators, to implement an

acceptable solution.

The CSPF has said that it believes a legislative solution to its funded status is necessary or that it will become insolvent in 2025, and we expect that the CSPF will continue to explore options to avoid insolvency. Numerous factors could affect the CSPF's funded status and UPS's potential obligation to pay coordinating benefits under the UPS/IBT Plan. Any obligation to pay coordinating benefits will be subject to a number of significant uncertainties, including whether the CSPF submits a revised MPRA filing and the terms thereof, or whether it otherwise seeks federal government assistance, as well as the terms of any applicable legislation, the extent to which benefits are paid by the PBGC and our ability to successfully defend legal positions we may take in the future under the MPRA, including the suspension ordering provisions, our withdrawal agreement and other applicable law.

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We account for the potential obligation to pay coordinating benefits to the UPS Transfer Group under Accounting Standards Codification Topic 715- Compensation- Retirement Benefits (“ASC 715”), which requires us to provide a best estimate of various actuarial assumptions, including the eventual outcome of this matter, in measuring our pension benefit obligation at the December 31st measurement date. While we currently believe the most likely outcome to this matter and the broader systemic problems facing multiemployer pension plans is intervention by the federal government, ASC 715 does not permit anticipation of changes in law in making a best estimate of pension liabilities.

As such, our best estimate of the next most likely outcome at the measurement date is that the CSPF submits and implements another benefit reduction plan under the MPRA during 2019. We believe any MPRA filing would be designed to forestall insolvency by reducing benefits to participants other than the UPS Transfer Group to the maximum extent permitted, and then reducing benefits to the UPS Transfer Group by a lesser amount.

We have evaluated this outcome using a deterministic cash flow projection, reflecting updated estimated CSPF cash flows and investment earnings, the lack of legislative action and the absence of a MPRA filing by the CSPF in 2018. As a result, at the December 31, 2018 measurement date, the best estimate of our projected benefit obligation increased by \$1.6 billion for coordinating benefits that may be required to be directly provided by the UPS/IBT Plan to the UPS Transfer Group.

The future value of this estimate will be influenced by the terms and timing of any MPRA filing, changes in our discount rate, rate of return on assets and other actuarial assumptions, presumed solvency of the PBGC, as well as potential solutions resulting from federal government intervention. Any such event may result in a decrease or an increase in the best estimate of our projected benefit obligation. If the uncertainties are not resolved, it is reasonably possible that our projected benefit obligation could increase by approximately \$2.4 billion, resulting in a total obligation for coordinating benefits of approximately \$4.0 billion as previously disclosed. If a future change in law occurs, it may be a significant event requiring an interim remeasurement of the UPS/IBT Plan at the date the law is enacted. We will continue to assess the impact of these uncertainties on our projected benefit obligation in accordance with ASC 715.

#### Other Actuarial Assumptions

Healthcare cost trends are used to project future postretirement medical benefits payable from our plans. For year-end 2018 U.S. plan obligations, future postretirement medical benefit costs were forecasted assuming an initial annual rate of increase of 6.0%, decreasing to 4.5% by the year 2022 and with consistent annual increases at that ultimate level thereafter.

#### Funded Status

The following table discloses the funded status of our plans and the amounts recognized in our consolidated balance sheets as of December 31st (in millions):

	U.S. Pension Benefits		U.S. Postretirement Medical Benefits		International Pension Benefits	
	2018	2017	2018	2017	2018	2017
Funded Status:						
Fair value of plan assets	\$39,554	\$41,932	\$26	\$183	\$1,284	\$1,333
Benefit obligation	(45,333 )	(45,847 )	(2,510 )	(2,792 )	(1,552 )	(1,651 )
Funded status recognized at December 31	\$(5,779 )	\$(3,915 )	\$(2,484 )	\$(2,609 )	\$(268 )	\$(318 )
Funded Status Recognized in our Balance Sheet:						
Other non-current assets	\$—	\$284	\$—	\$—	\$35	\$35
Other current liabilities	(20 )	(18 )	(195 )	(77 )	(4 )	(5 )

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Pension and postretirement benefit obligations	(5,759 )	(4,181 )	(2,289 )	(2,532 )	(299 )	(348 )
Net liability at December 31	\$(5,779 )	\$(3,915 )	\$(2,484 )	\$(2,609 )	\$(268 )	\$(318 )
Amounts Recognized in AOCI:						
Unrecognized net prior service cost	\$(1,018 )	\$(880 )	\$(21 )	\$(29 )	\$(14 )	\$(2 )
Unrecognized net actuarial gain (loss)	(3,967 )	(4,277 )	(32 )	(195 )		